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*Comparative Economic Systems*



THE MACMILLAN COMPANY  
NEW YORK BOSTON CHICAGO DALLAS  
ATLANTA SAN FRANCISCO  
MACMILLAN AND CO., LIMITED  
LONDON BOMBAY CALCUTTA MADRAS  
MELBOURNE  
THE MACMILLAN COMPANY  
OF CANADA, LIMITED  
TORONTO

# *Comparative Economic Systems*

**REVISED EDITION**

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UNIVERSITY OF ILLINOIS

**THE MACMILLAN COMPANY**

*New York*

*1949*

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PRINTED IN THE UNITED STATES OF AMERICA

## PREFACE TO THE REVISED EDITION

THE publication of a revision in 1949 of a textbook in Comparative Economic Systems which appeared originally early in 1944 should not require much explanation. The intervening years have brought increased insight into the problems of capitalism and alternative systems, detailed knowledge concerning the economic experiences of Soviet Russia in World War II and in the early postwar years, the beginning of the great experiment with partial socialism in Great Britain, the decline and fall of the fascist systems of Germany and Italy, and an increasing trend toward some form of collectivism in the United States and many other important countries. As a result, the issues involved in the study of comparative economic systems are now more than ever among the most lively and important faced by students and citizens.

The changes made in the book from the first edition to the second are primarily those which were dictated by the events noted above. Some of the sections dealing with capitalism have been expanded slightly to allow for the discussion of issues which have increased in importance in recent years, such as full-employment policy, the public debt, price control and rationing. A few sections on theoretical socialism have also been amplified to some extent. Sections dealing with Soviet Russia in the period up to World War II have been modified in the interest of greater accuracy and conciseness, and material has been added dealing with the economic experiences of Soviet Russia during the war, losses suffered as a result of the war, the goals of the Fourth Five-Year Plan, and the economic developments of the early postwar years. In connection with each important economic topic, a section has been added which discusses the aims, methods, and results of the program of partial socialism carried on in Great Britain under the auspices of the Labor Party in the last few years. Finally, all the sections dealing with the economic systems of fascism have been materially reduced in length, and the fascist systems have been considered together to a greater extent than formerly, rather than on a country-by-country basis.

The study of comparative economic systems on the basis of important economic topics, rather than by analyzing one complete economic system after another, has proved successful, and this approach is retained in the revised edition. The style of the book is unchanged, as are its general attitude and outlook. Although approximately half the material of the revised edition is either new or rewritten, deletions and condensations have almost balanced the additions, and the over-all length of the book has changed only slightly. As a result, it should be no more difficult for students to read or for teachers and classes to get over in the time available.

In the preparation of the revised edition, I have been assisted greatly by criticisms and suggestions given me by many teachers who have used the first edition in their classes, by colleagues on the staff of the Economics Department at the University of Illinois, and by large numbers of intelligent and interested students in my own classes. I am also much indebted to Miss Lois Jedlicka, who has typed the manuscript of the revised edition with painstaking care and has assisted with the tasks of indexing and proofreading.

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## PREFACE TO THE FIRST EDITION

THE study of comparative economic systems was interesting and profitable even in the old days when the only alternatives to existing capitalism were found in the theoretical systems of socialism and communism. With the development of the planned economy of Soviet Russia and the fascist systems of Italy and Germany, this study became important as well as interesting. Today questions in the field of comparative economic systems are of vital importance. They are questions of the hour. Differences between national economies played a significant role in producing the Second World War and in the conduct of that struggle. An understanding of them will be necessary to the construction of a lasting peace. The growing importance of the study of comparative economic systems has found expression in the development of courses in this field in colleges and universities all over the country in recent years. This book is intended primarily to serve as a textbook for such courses.

The approach to the study of comparative economic systems used in the present volume is distinctive. The textbooks already in use are content simply to analyze one economic system after another until the entire list of systems has been covered. It seems to me that it may be questioned whether this is the best method for effecting comparisons of economic systems, for students are likely to forget much of what they have read concerning earlier economic systems by the time they reach the systems which are treated later in the book. In studying the control of prices or the distribution of income in Germany under National Socialism, the students are handicapped by the fact that it has been from one to three months since these same topics were studied in connection with capitalism, socialism, or the Soviet Russian economy.

In the present volume the organization of the material is by economic topics rather than by economic systems. The topics covered in Part One, which deals with Comparative Economic Systems proper, include economic principles, economic institutions, government, the making of important economic decisions (whether by means of the price system, economic planning, or some combination

of these methods), the organization of production, agriculture, marketing, price control, and rationing, credit and banking, the distribution of income, the economic status of labor (and related topics such as social insurance, business cycles and unemployment, and population policy), international trade and economic self-sufficiency, and public finance. Each of these important phases of economic life is discussed in relation to capitalism (with the United States as the leading example), theoretical socialism, theoretical communism, and the actually-operating economies of Soviet Russia, Fascist Italy, and National Socialist Germany. Thus, the student learns about the economic institutions of all the economic systems at one point in the course, about the distribution of income in all the systems at another, about the handling of the agricultural problem in all the systems at another, and so on.

The advantages of this topical method of approach are several in number. The study of the principles and methods by means of which all the types of economic systems handle important individual phases of economic life and deal with leading economic problems facilitates the comparison of these systems and makes similarities and differences between the systems stand out clearly. Any danger that the student will lose sight of the forest as a whole in his study of the individual trees is minimized by the presentation of several chapters at the end of Part One which summarize and evaluate the various economic systems as complete entities. The use of the topical method of approach also helps to ensure that the discussion of the various systems will be comparatively thorough and well-balanced, whereas the organization of the subject by systems makes it at least possible that the discussion of each system will be confined largely to its most striking features and policies and that public finance or the distribution of income, for example, will be discussed in great detail in connection with one system and treated very lightly if at all in connection with another. Finally, the use of the topical method of approach makes it possible more readily to emphasize economic principles and economic theory in the discussion of economic systems, and the present volume is intended to give the student a good review of general economics as well as an understanding of comparative economic systems. It is hoped that the student will finish his study of this book with a better knowledge of general economics and of the way in which our capitalistic system operates than he had after completing his course or courses in eco-

nomic principles and problems,—and a knowledge acquired pleasantly and painlessly.

It is common, in books on this subject, to take it for granted that the students will have acquired an adequate knowledge of the capitalistic system and its method of operation before they approach the study of comparative economic systems. As a result, no section at all, or only a comparatively small one, is devoted to the analysis of capitalism as such. On the basis of my experience in teaching the course in comparative economic systems during the last ten years, this assumption concerning the students is frequently, if not usually, invalid. Believing that it is difficult to understand or evaluate other economic systems unless one has an adequate understanding of capitalism and confident that most students need additional work on the subject, I have definitely taken capitalism to be one of the systems to be analyzed and evaluated in the present book. Accordingly, considerable material is presented both with regard to capitalism in general and with regard to the capitalistic system of the United States in particular. Some of this material is rather elementary in character and will be familiar to students who are well prepared in general economics. Such material can be eliminated from discussion, of course, by instructors who feel that it is unnecessary, but in many cases it will be found that students can review the material with profit.

Part Two of this volume is given over to the discussion of Marxian Socialism. It covers such matters as the Marxian philosophy, interpretation of history, and concept of the state, theories of value, wages, surplus value, and class struggle, predictions concerning the future development of capitalism and its eventual breakdown, and prophecies with regard to the revolution, the dictatorship of the proletariat, and the eventual classless society of anarchistic communism. The section on Marxian Socialism is separated from the rest of the book because so much of it is an analysis and criticism of capitalism as it existed in Marx's time rather than a set of proposals with regard to an ideal system or systems which might replace capitalism. On the other hand, it was felt that a book on comparative economic systems would not be considered complete if it failed to present a discussion of Marxian Socialism. The analysis and evaluation of Marx's work is intended to be reasonably thorough and intensive, and yet an effort was made to keep the discussion on a level suitable for advanced undergraduate students of economics.

Throughout the book I have attempted to maintain an objective attitude and a moderate tone. Certainly I have not tried to serve as a super-salesman for any one type of economic system, nor have I tried to lend support to the impression, which many people have, that the capitalistic system of the United States is doomed. However, I am almost convinced that complete objectivity in the controversial field of comparative economic systems, whether on the part of authors or readers, is an unattainable ideal. As a result, I shall not be surprised if those readers who agree with my conclusions and opinions find my book highly objective in its treatment of economic systems while those who disagree with these same conclusions and opinions discover it to be strongly biased. Such a degree of objectivity as the book contains is real and not merely simulated. If I have presented a certain number of advantages or accomplishments for one type of economic system, I have not thought it necessary to present exactly the same number for each other type of economic system. In similar fashion, if I have assigned eight failures or weaknesses to a particular economic system, I have not considered it necessary to conjure up an exactly offsetting number of advantages or accomplishments in order to give the appearance of fairness. The evaluations of the various economic systems are intended to be thorough and sincere, and not mere listings of pros and cons.

My thanks are due to many persons for assistance in the preparation of this volume. I am indebted to my colleagues of the Economics Department of the University of Illinois for helpful suggestions and advice, to Merlin H. Hunter who has arranged my teaching schedules so that I would have an opportunity for investigation and writing, and has given me constant encouragement, to my many excellent students in classes in Comparative Economic Systems for valuable criticisms, to the several anonymous readers who analyzed and criticized the manuscript and made many worthwhile suggestions for its improvement, to many publishers who generously gave me permission to quote excerpts from their works, to Mrs. Leona Alexander and Miss Frances Sturz for their careful typing of the manuscript, and to my wife and daughter whose patience and understanding have been invaluable to the completion of this project.

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**P A R T I**



*Comparative Economic Systems*



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## CHAPTER 1

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### **ECONOMIC PRINCIPLES AND ECONOMIC SYSTEMS**

Most textbooks in the principles of economics pay very little attention to the subject of differences between economic systems. In some cases, no reference is made even to the existence of economic systems other than capitalism. In others, the existence of socialistic and fascist economies is recognized but economic principles are presented in such a way and the description of economic activity is of such a character that readers are led to believe either that the economic affairs of non-capitalistic systems are of no great importance or that these affairs are so much like those of our own capitalistic system that no separate treatment of them is required.

Today, of course, there is no excuse for a person to think that, because he has observed only the operation of our capitalistic system, no other economic systems exist or have existed. The events leading up to World War II and those of that conflict itself served to emphasize the fact that non-capitalistic economies were in actual and more or less successful operation. The war period found the fascist economies of Germany, Italy, and Japan arrayed against the capitalistic economies of the United States and Great Britain and the socialistic economy of Soviet Russia in a struggle to the death. The postwar period has witnessed the virtually head-on clash between the United States and Soviet Russia and the gradual emergence of a form of socialism in Great Britain. The question of the kind of economic system which we shall or should have in the United States in the postwar period is still very much at issue. Indeed, we hear many persons insisting that the basic institutions of our capitalistic system should be maintained and preserved in the postwar period while at the same time the federal government should attempt to guarantee the existence of full employment,

furnish a complete system of social security for all the citizens, try to reduce significantly the extent of inequality in the distribution of income, and follow other policies which might make it impossible to operate a capitalistic economic system in this country.

At the present time, the student of economic affairs can scarcely consider himself well informed unless he has some rather definite and accurate ideas as to how socialistic, communistic, and fascist economic systems differ from our capitalistic system. The present book is intended to furnish at least a part of the information which is necessary for this purpose. In Part I, we shall consider similarities and differences between various economic systems with respect to economic principles, economic institutions, governments as related to economic life, the ways in which decisions are reached on important economic matters, the practices and policies which are used in carrying out these decisions, and points of economic strength and weakness. Part II deals with the analysis and evaluation of the powerful Marxian criticisms of the operation of capitalistic economic systems and predictions as to the future of such systems. The study of Marxian Socialism is important in its own right, and it has had an important influence on various theoretical and actually operating economic systems.

### *Economic Principles of General Validity*

In beginning the study of economic systems, we shall concern ourselves first with the important question of whether the principles of economics, as ordinarily set forth, are valid for all types of economic systems, or have application only to capitalistic economies. The discussion which follows will show that many important economic principles, since they involve no assumptions as to the economic institutions which prevail in a given system, are as valid under socialism, communism, or fascism as under capitalism. However, there are a few economic principles which, though valid in a capitalistic economy, depend upon the existence of a certain set of capitalistic economic institutions for their validity and have no application in systems which lack these institutions. We shall turn now to a detailed examination of the first of these groups of economic principles.

**Scarcity and the Economic Problem** In the first place, economic activity rests upon the same general foundations in all economic

systems Economic activity arises everywhere out of the abundance of human wants and the scarcity of the direct and indirect means for their satisfaction Human wants are both great and growing If not unlimited, they are at least indefinitely expandible The commodities and services which can satisfy these wants are relatively scarce, and so are the productive agents (land, labor, and capital) which can produce the desired commodities and services The various grades and types of these productive agents usually have alternative uses, that is, they can be used in the production of a number of different commodities and services Thus, the economic problem in any system is that of allocating limited productive resources, which have alternative uses, to the satisfaction of great and growing human wants

Economic systems may differ with respect to the importance which they attribute to the problem of satisfying the economic wants of their citizens Under capitalism, it is assumed that the economic problem is primary and basic, that the best allocation of productive resources is that which results in the maximization of the commodities and services available for use, and that the achievement of this maximization would produce the highest degree of human welfare These latter assumptions are not completely justified from some points of view, as will be seen in Chapter 5, but they are made by many economists under capitalism The ideal theoretical systems of socialism and communism and the actual socialistic system of Soviet Russia seem to agree with these notions as to the most appropriate goals or ends of economic activity, but hold that these goals can be achieved most effectively by methods and practices quite different from those employed under capitalism On the other hand, the leaders of the fascist systems held that economic ends as such are of secondary importance and denied that welfare is achieved by the maximization of the commodities and services desired by individuals These leaders contended that the nation as a whole is not merely the sum of the individuals who compose it at any particular time, and that the nation or state may have ends which are quite different from those of the individuals of the system and which may actually be in conflict with individual interests The goals of the nation are of fundamental importance and must be achieved whether or not their realization is consistent with the enjoyment of the greatest possible quantities of commodities and services by individuals Thus, economic systems may differ with

regard to the objectives which should be sought as well as with regard to the methods which should be used in attaining given objectives

**The Law of Diminishing Productivity** Turning now to the discussion of specific economic principles, we recall that one of the most important of these principles is the Law of Diminishing Productivity This law states that *if the technology of production remains unchanged and equal successive units of some one agent of production are applied to a fixed amount of other productive agents, the average product per unit of the variable agent, after a certain point has been reached, will decline*<sup>1</sup> Is this general tendency one which will operate only under capitalism or may it be expected to operate in any type of economic system? The answer is obvious The principle in question has nothing to do with differences in economic systems Wherever the individual enterpriser attempts to increase production under the conditions specified by the law, he will encounter sooner or later diminishing increments of physical product and hence diminishing average product per unit of the variable agent The most powerful dictator under socialism or fascism is helpless to prevent the operation of this law He can no more keep it from functioning than he can regulate the ebb and flow of the tides

The reason for the universal validity of the Law of Diminishing Productivity is found in the fact that the law rests on no assumptions concerning economic institutions or activities of the government Its assumptions are purely physical in character and are such as may be realized in practice in any economic system Under the conditions specified in the law, diminishing productivity is encountered whether land and capital are owned privately or publicly, whether enterprises are run by private individuals or the government, whether individuals in charge of enterprises are motivated by the desire for maximum profits or maximum losses, whether economic conditions in general are competitive or non-competitive, and whether economic decisions are made on the basis of price relationships or by economic planning

**The Law of Comparative Advantage** The Law of Comparative Advantage or Comparative Costs is an economic principle which is in the class with the Law of Diminishing Returns It does not

<sup>1</sup>R. H. Blodgett, *Principles of Economics*, revised edition New York Rinehart and Company, Inc., 1916, p. 114

assume or depend upon any particular set of economic institutions. The only condition necessary for its operation is that the various nations should differ with respect to their endowments of the productive agents, that is, that some nations should have productive agents which other nations lack or should have large amounts of productive agents which other nations have in small quantities. If this condition is realized, some nations will have absolute or comparative advantages in the production of certain economic goods while other nations will have similar advantages in other fields of production. The Law of Comparative Advantage suggests that each nation will maximize the quantity of commodities and services at its disposal and achieve the highest possible standard of living if it produces only those economic goods which are best suited to its particular endowment of productive factors and obtains its other economic goods through international trade.

The conclusion which is often drawn from this principle—to the effect that countries will actually produce and export economic goods in the production of which they have the greatest comparative advantages or least comparative disadvantages, and will import other types of economic goods—is not universally valid. It will hold true only when the citizens of a country are left free to follow their own interests in matters of international trade. Any economic system, whether capitalistic or non-capitalistic, may decide to disregard the Principle of Comparative Advantage and produce at home certain goods which could be obtained more cheaply abroad. In fact, in order to be prepared for war or for some other reason, a nation may deem it wise to be as nearly economically self-sufficient as possible. While no nation is likely to achieve this goal completely, some nations can come fairly close to it. However, the Law of Comparative Advantage cannot be disregarded with impunity. The more closely a nation approaches the goal of economic self-sufficiency, the greater is the sacrifice which it must make in the form of a standard of living lower than that which could be achieved on the basis of international specialization and exchange. This penalty must be paid under capitalism, socialism, communism, or fascism. It can no more be avoided by a dictatorship than by a democracy.

*Principles of Production.* In general, economic principles in the field of production may be regarded as universally valid. In studying production, we learn that specialized production is more efficient

than non-specialized production, that large-scale production is often preferable to small-scale production, and that roundabout or indirect production (using large quantities of capital) is more advantageous than direct production. These productive principles depend in no way on economic institutions or forms of government. By following them, we obtain larger quantities of goods, a greater variety of goods, and in many cases a better quality of goods than could otherwise be secured. Wherever these productive results are deemed desirable, the principles in question tend to be followed.

In examining the various types of economic systems, we find these productive principles in widespread operation. Specialization by trades and tasks is characteristic of the economies of Soviet Russia and capitalist America, and was practiced in the fascist economies of Germany and Italy. The United States has some of the largest-scale productive units in the world, but other giants are found in Soviet Russia and Germany. The leaders of some economies condemn our evil private capitalists, but all economies use considerable quantities of capital goods in production. The large productive unit may be a corporation in one system and a governmental enterprise in another, but the advantages of large size are widely realized. The specialized workers may be employed by a private firm in one economy and by the government in another, but they specialize in any case.

*Saving and Capital Formation.* Large quantities of capital will not be available for use in production unless the process of saving and capital formation functions efficiently. This process is fundamentally the same in all types of economic systems. It cannot operate unless the available productive agents are somewhat more than adequate to provide a bare living for the people of the system. When it is able to operate, it involves, in a money sense, spending part of the money income of the economy, directly or indirectly, for capital goods rather than for consumers' goods. In the non-monetary sense, saving and capital formation require the allocation of a part of the productive resources of the nation to the turning out of capital goods rather than consumers' goods. The cost of obtaining capital goods, which will make for a more abundant life in the future, is the same in all economic systems. It is found in the necessity of going without at present the quantities of consumers' goods and services which could have been produced by the agents of

production which are actually allocated to the production of capital goods

Of course, there may be great differences between economic systems as to the mechanics of the process of saving and capital formation. In a socialistic society, the planning board at the head of the economic activities of the economy may decide the respective portions of the national income, which are to go into consumption and capital formation, allocate arbitrarily existing productive agents to these two great divisions of production, handle the problem of distributing the capital goods which are produced among the various industries of the economy, and see to it that all the consumers in the economy, since they have sacrificed to make capital formation possible, share in the benefits which are realized later in the form of increased quantities of commodities and services. In a capitalistic system, individuals and organizations may be left relatively free to save or not to save and to put aside any quantity of funds which they consider most appropriate on the basis of interest rates and other price and non-price considerations. The production of capital goods is undertaken not on the basis of governmental fiat but on that of orders received from firms which have capital funds to spend. The allocation of capital funds among the various industries may be left to investment banking institutions and to corporations which have earnings to reinvest, and a large part of the eventual benefits of capital formation may go to the limited group which has made capital funds available. However, in spite of all such differences, the basic process of saving and capital formation is the same in all economic systems.

*Commercial and Investment Credit* Credit involves the turning over to a debtor of some valuable consideration (money or goods) by a creditor at a given time in return for a future equivalent to be furnished by the debtor. The use of commercial and investment credit is basic to the operation of a capitalistic economic system but both of these types of credit are also likely to be found in other types of economic systems. The essential principle involved in each of these types of credit depends upon modern productive methods. When production is specialized, large-scale, and roundabout, it consumes a considerable amount of time and must often take place in anticipation of demand rather than on order. Under these conditions, it is completely impossible to make the various expenses which must be met coincide in time with the receipt of payments for the

final products Raw materials and supplies must be purchased in advance of production, expenditures for labor, power, and other things must be made as production proceeds, and some time later payment is received for the finished product In the meantime, someone must "wait", that is, extend commercial credit by giving up money or goods at present in return for an equivalent value later.

Under capitalism, it is customary for commercial banks to do the waiting, by extending funds with which business enterprises can meet expenses during the productive process, but the existence of banks is not necessary to the existence of commercial credit Under certain conditions, a productive enterprise itself may finance its productive process, meeting all expenses when due and waiting for reimbursement until the finished product has been sold and paid for Again, sellers of materials and supplies might trust the enterprisers in manufacturing until the final product had been completed and sold, or the government, acting for all the people, might take charge of the necessary details of financing Regardless of such differences in administrative procedure, the existence of commercial credit arises out of the use of modern productive methods, and it will be found in any economic system in which these methods are used

A similar condition exists in investment credit Modern productive methods require usually the employment of large quantities of fixed capital goods The production of such durable capital items as machines and factories involves certain expenses which must be met ordinarily within a comparatively short period of time, but the durable capital goods themselves give off their benefits over a long period of time, and sometimes many years, instead of all at once Again, it is clear that the costs and the resulting receipts of income cannot be made to coincide in time and that someone must make advances at the beginning of the process and wait for a long time for reimbursement As in the case of commercial credit, there may be several choices as to the identity of the persons or organizations who will do the actual waiting, but investment credit will exist in some form or other wherever durable capital goods are used, whatever the nature of the economic system and whether or not there are specialized banking institutions for dealing with investment credit

*Principles of the Theory of Value* Some of the principles which are usually set forth under the general heading of the theory of

value may also be expected to be valid in any type of economic system An example is the Law of Diminishing Utility, which holds that *the intensity of a person's desire for a unit of a given economic good varies inversely with the amount of the good which he already has in his possession, and diminishes progressively as additional units are acquired*<sup>2</sup> This principle is clearly just the psychological counterpart of the Law of Diminishing Returns, and it rests upon no assumptions as to the nature of the economic system and its institutions Under any economic system, with a small amount of a good on hand, the strength of the individual's desire for an added unit of the good would be relatively great, while with a large amount of the good already in his possession the desirability of an added unit would be relatively small

The Law of Diminishing Utility is usually presented as an aid to the understanding of demand in connection with the determination of prices, but it would be valid even if individuals did not have money incomes which they could spend for the various commodities and services which they desire If the government of a non-capitalistic economic system merely issued successive shirts to the male citizens of the economy, it is reasonable to suppose that each consumer would value one shirt less when he had ten than when he had only two, if all the shirts were identical in kind and quality Even in a communistic system, in which the individual acquired goods as he needed them by helping himself without charge at a public storehouse, the knowledge that the storehouse contained more pairs of standard shoes than the citizens were likely to be able to consume for some time would probably cause the individual to value any one pair of shoes less than would be the case under conditions of more limited supply The Law of Diminishing Utility is only the economic expression of the tendency of the human organism to make lessened responses as a certain stimulus is repeated

The Law of Demand in economies states that *the quantity of an economic good which buyers are willing to purchase varies inversely with the price, in a given market at a given time*<sup>3</sup> Wherever individuals have money incomes which they may spend on the various economic goods which they desire, the existence of an unusually low price for a good on a given day tends to produce a large volume of sales while an unusually high price tends to curtail the number

<sup>2</sup> *Ibid.*, p. 218

<sup>3</sup> *Ibid.*, p. 215

of sales made In socialistic or fascist economies, as well as in the United States, bargain days and bargain prices produce large crowds of buyers and an increased volume of transactions Of course, in an economic system in which individuals had no money incomes, and commodities and services had no prices attached to them, the Law of Demand would be quite irrelevant, (although the psychological assumptions implicit in the Law would still apply), but such types of communistic economic systems exist today only in the realm of theory

In any system in which the Law of Demand would be valid, we should expect the demands for some economic goods to be "elastic" while those for other economic goods would be "inelastic" For much the same reasons as under capitalism, increases in the prices of some goods would cause a more than proportionate decrease in the quantities which buyers were willing to take, while price decreases would lead to a more than proportionate increase in purchases The demand in such cases is said to be elastic In the opposite case of inelastic demand, a given increase or decrease in price would lead to a less than proportionate decrease or increase, respectively, in the quantity of the good which buyers would be willing to purchase As long as economic goods differ with respect to the availability of substitutes, the part which each plays in the budget of the average person, the number of uses to which each may be put, and dispensability, both elastic and inelastic demands may be expected to exist in an economy in which individuals have money incomes to spend for a variety of economic goods

The principle of opportunity or alternative costs is of importance in many sections of the study of economics, as our discussion of the process of saving and capital formation has indicated, but the principle itself is often presented as part of the discussion of costs in connection with price determination Whenever agents of production have alternative uses and are scarce in relation to human wants for the goods which they are capable of producing, the cost of getting more of one economic good in order to satisfy a given want more completely is found in the necessity of giving up the other commodities and services which could be produced by the additional productive agents which will go to increase the output of the first good In fact, the opportunity cost doctrine deals with cost in the most fundamental sense of that term All economic systems must be concerned with the problem involved in the principle of oppor-

tunity costs, even though some economies need hardly worry about costs in any other sense

### *Economic Principles of Limited Validity*

We have seen that the economic principles which we may expect to be valid for all types of economic systems are those which make no assumptions concerning the economic institutions which prevail in the surrounding economy. Many of these principles are laws of nature or of human nature before they are economic laws. Economic principles which assume openly or tacitly the existence of the economic institutions of capitalism will be valid only under capitalism or in other economies, if any, in which institutions similar to those of capitalism exist and are allowed to operate. We shall deal with several principles of this kind in the present section.

**The Law of Long-Run Competitive Price** Perhaps the principle which the student is most likely to remember from his study of the theory of value or price determination is the Law of Long-Run Competitive Price, which holds that *the price of an economic good in the long run under competition, as determined by demand and supply, tends to equal cost of production per unit*.<sup>4</sup> Competition, as used in this connection, refers to several conditions of the market for an economic good, including the presence of such a large number of buyers and sellers that no buyer or seller can affect the price of the good by his actions in the market, the absence of agreements, combinations, and conspiracies between sellers or between buyers with respect to prices or quantities to be bought and sold, the existence of reasonable knowledge and information among buyers and sellers, and non-interference by government in the process of determining prices and quantities to be bought and sold. It is only under these conditions that the Law of Long-Run Competitive Price is supposed to work even in a capitalistic system, which means that it is inapplicable in numerous situations under capitalism.

But the law in reality assumes more than the competitive conditions just described. As the very description of conditions of competition shows, it is assumed that productive wealth (land and capital) is under private ownership and control, which means that the institution of private property exists. The buyers and sellers

<sup>4</sup> *Ibid.*, p. 273

are assumed to be motivated economically and they try to buy cheap and sell dear Again, it is implied that business men are free to enter or leave a particular industry at will, and that they can produce as much or as little of a given economic good as their self-interest seems to indicate, which means that the institution of freedom of enterprise is also functioning

It is, of course, apparent without explanation that laws of this sort, which are concerned with the determination of prices, would be entirely irrelevant for an ideal communistic society which had eliminated money and prices from its economic activities and in which no exchanges of goods in the ordinary sense were carried on However, the law in question means just about as little for theoretical socialism or socialism as actually operated in Soviet Russia Under socialism, productive wealth is almost entirely owned by society as a whole, as represented by government, only the government has freedom of enterprise in any true sense, economic motivation is limited to the desire to obtain high rather than low wages from employment with the government, and competition, as we have described it, would be conspicuous by its absence Under these conditions, we should look in vain for the operation of the Law of Long-Run Competitive Price

At this point, an objection might be raised That is, it might still be thought that the Law of Long-Run Competitive Price would have some validity under socialism Will the government of socialism, representing (presumably) society as a whole, be able to disregard the relationship between prices and costs of production in running its many industries? Will it not have to set prices for its various products which will at least cover the costs of producing them and putting them on the market? In this connection, there are at least two points which must be given attention sooner or later In the first place, it is very difficult for the government under socialism to know what its costs of production are Since the government is the only important demander of the productive agents in general and is also the only important owner and supplier of land and capital, it seems to most economists that there is clearly no real market for these agents and that any prices placed on land and capital for the purpose of computing costs are bound to be rather arbitrary Since there are others who believe that rational costing and pricing under socialism are possible, even in the absence of genuine markets for the agents, we shall deal with this complex

subject in a later chapter and be satisfied here with merely raising the question

In the second place, even though prices and costs can be established in some way or other under socialism, the relation between them does not seem to be particularly binding on the government. Since the government (or its planning commission) will establish prices of finished goods and costs for the productive agents, it should be possible to make the price of a good cover the cost assigned to its production if this result is desired. But other results may seem more important. The government may decide that the public welfare requires the increased production of some article, whose price is already failing to cover its costs, and the lowering of its price. In another case it may decide that the production of another article should be abandoned in the public interest, even though it is selling readily at a price which more than covers costs. Such decisions would be difficult, if not impossible, for private enterprisers to reach under capitalism, for, with prices and costs determined by the market, the relation between them is important to these enterprisers. The price-cost relationship means next to nothing to a socialized government or planning board, which is the only important enterpriser and determines both prices and costs itself, for it can always make these two variables equal if it wishes.

In fact, it is not even necessary for the government under socialism to cover cost over the operation of the economy as a whole, unless it wants to. One of the most useful things to learn in the study of comparative economic systems is the fact that considerations of money profit and loss mean nothing practically to an economic system as a whole or to the government which operates such a system. Money profit and loss are individualistic concepts. If an individual enterpriser under capitalism makes a money profit, he gains, because his relative command over the real income of society is increased. Similarly, if he sustains a money loss, his relative command over the real income of society is decreased. But a nation as a whole can never enjoy more than its total real income, whether that income was produced with a money profit or with a money loss. There is nothing about a money profit made by a socialized economy which will increase its total real income by one iota nor will a money loss sustained by the society as enterpriser decrease this real income.

The operation of the whole economy at a money loss will then

have no serious implications It will mean, in effect, that the government has paid out more for costs of production (wages fundamentally) than it has received from the sale of all sorts of commodities and services This might be serious if the money income receivers of the economy were free to bid up the prices of the goods offered on the market, but this privilege is denied by the fact of price control by the government The net effect is merely to give workers more money than they can find a way to spend on commodities and services For reasons which have been suggested, the government would have no incentive to operate the whole economy at a profit under socialism In fact, it would be a rather difficult feat to do so, since it would require that the sum total of commodities and services be sold to consumers for more money than the total paid out by the government to the people as producers Thus, the government under socialism, though a great monopolist in a sense, would have little or no incentive or ability to follow the economist's Law of Monopoly Price, which suggests that the monopolist conducts his business in such a way that he makes the greatest possible total net (money) profit

*The Principle of Output Determination* Another principle of price determination which would not be valid in all types of economic systems states that the individual enterprise, under any condition of the market, will carry output in the intermediate period to the point where marginal cost and marginal revenue are equal To carry output farther would mean to produce some units of product which would add more to the firm's outgo than to its income, while to stop short of the designated output would mean a failure to produce some units of product which would add more to the firm's income than to its costs Clearly, then, the best financial result will be obtained by producing the output at which marginal cost and marginal revenue are equal

This principle, however, while it does not assume the existence of competitive conditions in the market, does assume that enterprises are privately owned and operated and that the enterpriser desires to obtain maximum profit or minimum loss from the operation of his business In other words, the principle implicitly assumes the existence of private property in the means of production, freedom of enterprise, and economic motivation There is no reason to think that the production of any commodity will necessarily stop at the output suggested in any economic system in which

these institutions of capitalism do not exist or in which they are rendered ineffective by constant governmental interference and control even though they may be nominally present.

Under socialism, for example, with prices and costs rather arbitrary to start with, with enterprises owned and operated by the government, and with the managers of enterprises desiring to fulfill the economic plan for physical volume of production rather than to make money profits or avoid losses, the output of an enterprise may exceed or fall short of that which would be sought by an enterprise under capitalism. The governmental planning board may decide that the economy should supply all its own needs for a particular article and merely order the managers, who are direct servants of the state, of the enterprises producing the good, to carry production to the desired point. Or, deciding that other articles are temporarily more important to the economy as a whole, the planners may decree that the enterprises in a given industry should operate at a very low rate or not at all in spite of the fact that the enterprises have large facilities for production and their product is greatly desired by the people.

*The Productivity Principle of Income Distribution.* In the field of the distribution of income, one of the best-known economic principles is that which holds that, in the long run under competitive conditions, the rate at which any agent of production is remunerated is determined by demand and supply conditions so that it tends to equal the marginal productivity of the agent. In this connection, marginal productivity is the money value of the marginal product, or the amount of product which would be lost if any one of the many like units of the productive agent in question were withdrawn from production. There is no doubt that this principle of income distribution is valid under the assumed conditions, but the conditions which are assumed are really so numerous and unlikely to be realized under actual conditions of the market that there is some question as to the practical significance of the principle even under capitalism. In order for the principle to operate, the people who demand and supply each productive agent must be very numerous, each demander and supplier of the agent must be independent of every other such person and must enter into no agreements or conspiracies which limit the market, there must be reasonable intelligence and information on both sides of the market, the units of the productive agent must be mobile between

occupations and, if possible, between places, the government must not interfere with the determination of rates of remuneration for the agent by the forces of demand and supply, and the enterprisers who demand the productive agent must sell their own finished products under conditions of competition. These assumptions are made openly. In addition, the principle under discussion tacitly assumes that the productive agents are privately owned and controlled so that they may be turned over to any enterprisers on the basis of the rates of remuneration offered, that the enterprisers who demand the productive agents are quite free to use them to produce for the market whatever commodities and services may have greatest exchange values, and that the people who demand the productive agents and those who supply them are for the most part economically motivated and desirous of pecuniary gain. In other words, the principle assumes the existence of such capitalistic institutions as private property, freedom of enterprise, and economic motivation.

If a purely communistic society, which holds that each individual should produce according to his ability and receive real income according to his needs, could actually operate, it is clear that the principle of income distribution which emphasizes marginal productivity would have no significance. Much the same conclusion must be reached in connection with a more moderate socialistic economy. With land, capital, and the direction of economic activities in public hands, interest, rent, and profits would accrue to the community as a whole and not to particular private individuals. Money wages for workers would be paid (and are paid in Soviet Russia) but it is very doubtful that they would be paid on a strict basis of productivity. In the first place, it would be very difficult to determine the value of the products of labor. The government, acting for society as a whole, would own and supply land and capital, it would be the only important demander of all the productive agents including labor, and it would be the only important supplier of finished goods on the market. The prices of finished goods would presumably be determined by some planning agency and not by the action of innumerable buyers and sellers on the market. Thus, while the products of labor would certainly have prices, these prices might be far from those which would actually prevail in a relatively free market for the same finished goods. The question of whether a socialistic economy, in the absence of a free market, could nevertheless achieve prices for finished goods and

costs for productive agents similar to those which would exist in a free market is an interesting point in theory and one which will be discussed in Chapter 5. For the present, it is only necessary to point out that a socialistic economy might be unwilling to use such prices and costs, even if they could be achieved in some manner or other.

In the matter of wages, this means that the economy might be unwilling to tolerate the degree of inequality in the distribution of money income that would result from the payment of wages on a strict basis of productivity. Wages are both a reward for something that has been accomplished and an incentive to get something done, and the emphasis might be on the latter aspect in a socialistic economy. That is, differences in wages might be set up largely for the purpose of inducing the labor supply to distribute itself among the various occupations and industries in a manner appropriate to the production of the kinds and quantities of commodities and services which the leaders or planners of the economy deemed socially desirable. With marginal productivity as indeterminate as it might well be under socialism, the wage differentials necessary to effect the desired distribution of the labor supply might differ somewhat from those which would prevail on a pure productivity basis.

Under fascism, it might be thought that conditions would be favorable for the operation of the principles of price determination and income distribution which we have just been discussing, for the economic institutions of fascism are at least nominally the same as those of capitalism. However, these capitalistic institutions are allowed to operate under fascism only to the extent that the economic interests of individuals are presumed to be in harmony with those of the state or nation. In all other cases, fascism stands for governmental interference and regulation to insure that the goals of the nation, rather than those of private individuals, will be achieved. Under such conditions we must be very skeptical as to the validity of economic principles that depend for their operation upon the full-fledged existence of the economic institutions of capitalism. A great degree of governmental interference in large sectors of the economy will make it impossible ordinarily for the economic principles in question to operate satisfactorily in other parts of the economy.

*The Quantity Theory of Money* The Quantity Theory of Money is considered by some writers as an economic principle which is

valid in any kind of economic system. Though it is stated in various ways, it says, in general, that the price level varies directly with the quantity of money and credit in circulation, if the velocity of circulation of money and credit and the volume of trade remain unchanged. That is, if velocity of circulation is constant, an increase in the quantity of money and credit in relation to the volume of trade will bring about a rise in the general price level, and vice versa.

This principle apparently deals only with broad economic forces such as will exist in any economic system and makes very few, if any, assumptions concerning economic institutions. Actually, however, the principle seems to require at least the assumption that the people who come into the possession of the increased quantities of money and credit will be free to use them to bid up the prices of things in general. In any economic system in which the government rigidly controls the prices of all commodities and services, either by regulation from outside or by being the direct controller of economic agents and processes, the individuals of the system may be unable to use any increased amounts of money income which they receive so as to bid up the prices of commodities and services. In such a situation, as we have seen, the increased quantities of money may merely lie idle in the pockets or homes of individuals and there may be nothing for which the money can be spent.

Even here, however, one could argue that money which cannot be spent for anything is not really in circulation or that the velocity of circulation of money in general is bound to be reduced by the presence of large quantities of idle funds, so that conditions specified by the principle are not present. It may also be argued that, in a socialistic or fascist economy in which prices are rigidly controlled, the government is likely to bring about a rise in the controlled price level if it has seen fit to permit increased money incomes to find their way into the possession of the citizens. In some cases, however, this might not be true. At any rate, there are economic systems in operation in which considerable increases in the quantity of money and credit in the hands of the citizens do not always (and certainly do not automatically) bring about increases in the general price level.

**Conclusions** The discussion of the present chapter has indicated that the major principles of economics must be given a rather clean bill of health with respect to their validity and applicability.

under various kinds of economic systems. Most such principles, being based on broad physical economic conditions, are not concerned with differences in systems, but a few principles, especially in the fields of value and distribution, depend directly upon the existence of a considerable range of capitalistic institutions for their validity and cannot claim much, if any, significance in situations in which these institutions are absent. On the whole, it is clear that we should have little to talk about in connection with economic systems, if the various systems were as nearly alike in other respects as they are in the matter of the economic principles which are valid in each system.

The present chapter has also suggested some of the respects in which we may expect economic systems to differ. Economic institutions are by no means the same in all economic systems, and governments differ both in organization and with respect to the part which they play in the economic life of the systems. As a result of differences in government and economic institutions, even economic systems which are apparently seeking the same final goals differ with respect to the organization of economic life, and further differences of these kinds may be expected between systems which do not agree as to the economic goals which are appropriate. In the next chapter, we turn to a comparison of the various economic systems on the basis of their economic institutions.

#### QUESTIONS

- 1 "Some economic laws or principles are valid in all types of economic systems while others are valid only in particular systems." Explain the difference between these two general classes of economic laws, and give examples of each type.
- 2 Compare the Law of Diminishing Returns with the Law of Long-Run Competitive Price with regard to the matter of validity in all types of economic systems.
- 3 Discuss the relative importance of economic principles and economic institutions in the study of differences between economic systems.
- 4 "If all economic systems were as nearly alike in other respects as they are with regard to the matter of the economic principles which are valid within these systems, there would be little point in studying economic systems." Discuss.
- 5 'The Law of Diminishing Returns would be important in a socialistic economy, but the Principle of Output Determination would be of no significance' Do you agree? Explain.

- 6 "Producers in any economic system would have to pay attention to the Law of Demand and to the elasticity of demand" Discuss
- 7 "Opportunity or alternative costs have the same significance in all economic systems, but the importance of money costs of production varies widely from one economic system to another" Explain
- 8 "The process of saving and capital formation is fundamentally the same in all types of economic systems" Show whether you agree
- 9 Why are both commercial and investment credit likely to be found in all types of economic systems?
- 10 "In a socialistic economy, the money prices of economic goods in general, if not those of particular economic goods, would have to be high enough to cover money costs of production" Do you agree? Explain
- 11 "In all economic systems, the owners of productive agents will tend to receive income on the basis of the marginal productivity of these agents" Discuss
- 12 Will the general price level in all economic systems tend to vary directly with the quantity of money and credit in circulation?

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## CHAPTER 2

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### **ECONOMIC INSTITUTIONS**

WHILE most of the economic principles which apply to capitalistic economic systems are valid in other types of systems as well, the economic institutions of capitalism either do not exist or are not allowed to operate freely in other systems. For our purposes, we may accept the dictionary definition of an institution as a practice, custom, or convention which is a material and persistent element in the life or culture of an organized group. It may or may not be consciously approved by society and organized and maintained through prescribed rules and agencies. Economic institutions, then, are habitual ways of reacting, in certain economic situations and with respect to certain economic phenomena, some of which rest on a basis of custom and tradition while others are formally recognized through legislative enactment.

*The Fundamental Significance of Institutions.* Differences in economic institutions are so important in connection with economic systems that definitions of these systems are usually stated in terms of institutions. A capitalistic system is defined in terms of private property, the profit motive, freedom of enterprise, the market mechanism, and competition, or some combination of these factors, while another economic system, such as socialism, is defined in terms of the modifications which it would make in some or all of these institutions. For example, it has been said that "A capitalist *industry* is one in which the material instruments of production are owned or hired by private persons and are operated at their orders with a view to selling at a profit the goods or services that they help to produce. A capitalist *economy*, or capitalist system, is one the *main part* of whose productive resources is engaged in capitalist industries".<sup>1</sup>

<sup>1</sup>A C Pigou *Socialism versus Capitalism* London Macmillan and Company, Ltd., 1937, p. 2

Again, we are told that "By this word *capitalism* we mean an economic system under which the fields, factories, and mines are owned by individuals and groups of individuals These means of production, as they are called, are worked by those who do not own them for the profit of those who do Under capitalism, it is profit-making, not love, that makes the world go round For it is the expectation of profit which induces those who own the above means of production to permit them to be used "<sup>2</sup> Finally, "The method of a capitalist society is the system of production for profit and exchange upon the market, modified by monopolistic combinations of capitalists, by trade-unions, and by such occasional and irregular intrusions of deliberate social intervention as tariffs, marketing boards, railway-rate regulation, factory acts, social insurance, etc "<sup>3</sup>

On the other hand, "A socialized industry is one in which the material instruments of production are owned by a public authority or voluntary association and operated, not with a view to profit by sale to other people, but for the direct service of those whom the authority or association represents A socialized system is one the *main part* of whose resources are engaged in socialized industries "<sup>4</sup> Such a system involves the elimination of private profit-making, the public or collective ownership of the means of production, and central economic planning for the common good (in some loose sense) Again "Socialism, as I understand it, means four closely connected things—a human fellowship which denies and expels distinctions of class, a social system in which no one is so much richer or poorer than his neighbors as to be unable to mix with them on equal terms, the common ownership and use of all the vital instruments of production, and an obligation on all citizens to serve one another according to their capacities in promoting the common well-being "<sup>5</sup> Finally, "Socialism is an economic organization of society in which the material means of production are owned by the whole community and operated by organs representative of and responsible to the community according to a general economic plan, all members of the community being entitled to

<sup>2</sup> John Strachey, *How Socialism Works* New York Modern Age Books, Inc., 1939, p 16 Reprinted by permission of the author

<sup>3</sup> From *Economics of Socialism* by H D Dickinson, Clarendon Press, Oxford, p 3 Reprinted by permission of the publishers

<sup>4</sup> A C Pigou, *Socialism versus Capitalism*, p 3

<sup>5</sup> G D H Cole, *The Simple Case for Socialism* London Victor Gollancz, Ltd., 1935, p 7 Reprinted by permission of the publishers

benefit from the results of such socialized planned production on the basis of equal rights" <sup>6</sup>

In similar fashion, we could define or describe communistic and fascist economic systems in terms of the institutions which they have or in terms of the ways in which they would modify the fundamental institutions of capitalism. However, we shall leave the nature of these systems to be understood from the description of their institutions later in this chapter and shall turn now to an analysis of the economic institutions of capitalism. In doing so, we shall limit ourselves to a relatively small number of institutions which seem really fundamental to the operation of a capitalistic economy.

### *Economic Institutions of Capitalism*

**Private Property** The institution of private property is so basic to capitalism that few definitions of that type of economic system are ever constructed without some reference to this institution. Private property is really a group or bundle of rights extended to the individual by society as a whole through a great variety of legal sanctions. Under its operation, the individual is entitled to use and control the economic goods which he acquires, to exclude other people from using them, and to decide usually how they shall be disposed of after his death. It is likely to include freedom of contract, or the right to bind oneself or one's possessions to the fulfillment of certain future conditions, and contracts freely made by competent and presumably equal persons are enforceable at law. The individual may abuse, as well as use, his wealth if his activities will not interfere with the equal rights of other persons. These various rights included under private property were not all acquired at once. Indeed, many writers look back to an ancient time when the institution did not exist and trace its beginning to the development of an economic surplus above the bare needs of subsistence of primitive groups. The various parts of the institution were added on one by one and even more gradually came to receive definite legal sanctions.

Many theories have been developed to explain and justify the existence of the institution of private property. Years ago, many

<sup>6</sup> From *Economics of Socialism* by H. D. Dickinson, Clarendon Press, Oxford, pp. 10-11. Reprinted by permission of the publishers.

people regarded private property as of natural origin, a natural right of man, which must necessarily exist. This idea still exists today to some extent, and especially among persons who own large quantities of wealth, but there is little to support it. The absence of private property in a state of nature and under primitive conditions suggests that the institution is definitely a creation of man in society. The explanation of private property as natural reveals merely a tendency on the part of many people to characterize whatever now exists and has long existed as natural. The labor theory of property was another early explanation of the institution. Man was supposed to have property rights in various objects of wealth because his labor had been responsible for the creation or production of these objects. As Adam Smith put it, "The property which every man has in his own labor [was] . . . the original foundation of all other property." This theory undoubtedly had some validity under the relatively simple conditions of the early days of modern capitalism when men had produced actually much of the wealth which they owned. However, it could be pointed out always that men had not produced the soil and other natural resources to which the institution of private property applied, and today, when people own so many things which cannot possibly be interpreted either directly or indirectly as the products of their labor, the theory has comparatively little standing.

In more modern times, private property came to be explained and justified on the basis of the social welfare theory. According to this theory, private property rights are granted by society as a whole to its individual members because it is assumed that all the members of society will be living under better conditions if each is granted these particular rights. This assumption was made because private property furnished an incentive to economic activity and to the accumulation of capital and other durable objects of wealth. If individuals were not protected in the use, control, and disposal of the economic goods which they acquired, the other institutions of capitalism, such as freedom of enterprise and economic motivation, would mean very little, and the capitalistic economy would be backward and unprogressive for lack of capital. That is, in the absence of private property, economic activity would be directed toward the acquisition of articles for immediate consumption or of goods whose large value and small bulk would permit them to be moved quickly and easily if some stronger person threatened to

appropriate them. Thus, it was held, a capitalistic society can be progressive and can accumulate maximum quantities of wealth (especially capital) only under the institution of private property.

This theory with regard to private property seemed rather valid in the early days of modern capitalism when the outstanding economic fact was the inability of the productive processes of the system to furnish enough commodities and services for the consumption of the people and when, consequently, the increased production of commodities and services could be seen to be closely related to increased human welfare. However, as the productive operations of capitalism have increased in scope and efficiency, the problem of the distribution of the possessions of society among its individual members has increased in relative importance while that of securing further increases in production has declined. Today, when the wealth of our capitalistic system is concentrated to an amazing extent in the hands of a relatively small number of persons while millions of others own almost no wealth, the beneficent influence of private property on the social welfare is sometimes called into question. We should also remember that human beings have some wants (sometimes called "non-economic" wants), such as the desire for security, health, or self-expression, which are not always readily expressed in the market place. Such wants are not always more completely satisfied by the increasing production of marketable commodities and services, and in some cases they may be actually more pressing and less completely satisfied as production expands toward the maximum. In other words, economic welfare in the limited sense is not the only kind of welfare, and the social-welfare theory of private property is under suspicion even if private property does have the effect of making for the increased production of commodities and services and the accumulation of capital. At present, the theory of social welfare in connection with private property is becoming, at the most, one of social expediency, which suggests that, taking the bad effects with the good, the institution of private property is more expedient than any other alternative which is available for dealing with the relationships between individuals and wealth.

*Restrictions on Private Property.* While the institution of private property is said often to confer on individuals the right of exclusive use and control of the economic goods which they acquire, it is clear that, since property rights are conferred by society as a whole,

upon its individual members, these rights can be modified and limited by social action In practice, even under capitalism, property rights are often restricted severely by the action of larger or smaller social groups or governmental units To take one example,

In the case of a city lot the owner is restricted by a vast array of codes regarding the use of the area He must place the front wall of the building on a "building line," the structure must be smaller than a certain maximum in size and larger than a certain minimum in cost, he cannot mine coal from beneath the surface or keep chickens or cattle upon it, he must provide access to official appraisers who periodically determine the value of the land and buildings for tax purposes, and he must contribute regularly in taxes to the cost of protecting his possession, maintaining access to it (streets and highways), bringing water to and draining sewage from it, and providing regular inspection to see that all requirements imposed by the group are met<sup>7</sup>

Restrictions which differ from the above only in scope and complexity apply to many other articles of wealth which individuals hold under the institution of private property Moreover, if the citizens of a capitalistic system decide that inequality in the distribution of income is becoming too great, they may, through their elected representatives, limit the rights of individuals to use and enjoy their money incomes by means of a progressive tax applicable to these incomes Similarly, if it appears that the inheritance of wealth or of claims on wealth is tending to produce an undesirable degree of concentration of ownership in the hands of a relatively small number of individuals, this part of the institution of private property may be modified, through inheritance taxation or otherwise, or even eliminated However, except for such restrictions and modifications, a capitalistic economic system endeavors wholeheartedly to protect the possessions of the individual from encroachment by governmental units or by other individuals For this reason, the limitations and modifications of private property through group action must be considered merely as exceptions to the prevailing rule in the capitalistic system

*Public and Corporate Property* We must not suppose that, because the institution of private property operates in a capitalistic system, all wealth is owned and controlled by private individuals as such There is actually a great deal of public property within most capitalistic systems Where public property exists, the exclusive

<sup>7</sup>R A Dixon, *Economic Institutions and Cultural Change* New York The McGraw-Hill Book Company, Inc., 1941, p 53

control of wealth is exercised by a larger or smaller group of individuals through some governmental unit or other, and the individuals within the group which the governmental unit represents ordinarily have equal rights to use the wealth in question Streets and roads, sidewalks and street lamps, parks and public buildings are examples to which the concept of public property applies Moreover, actual productive plants or industries may be owned sometimes and operated by various governmental units, as representatives of the body of citizens, even under capitalism

A great deal of the wealth of a capitalistic economy, such as the United States, is not owned directly either by private individuals or by public bodies, but rather by corporations Corporate property is distinctly a hybrid type Shares of corporate stock are, of course, owned by private individuals, but these shares are claims only against the general wealth of the corporation and not against specific objects of wealth, and the part owned by one individual cannot be separated from the parts owned by other individuals The ownership of corporate shares by numerous individuals makes corporate property resemble public or group property, in so far as the mere fact of ownership is concerned However, the control of corporate wealth by particular individuals makes corporate property resemble private property to some extent, except that the individuals who actually control corporate wealth are able to manage and direct the wealth which belongs to other individuals (bondholders or non-controlling shareholders) as well as their own

It is estimated that corporations control something like 60 to 65 per cent of the total volume of business in the United States and own about 80 per cent of all business wealth In 1946, 1000 large corporations owned about 55 per cent of the total assets of all corporations in manufacturing, and the 200 largest owned 44 per cent of the total<sup>8</sup> An estimate of several years ago suggested that only 11 per cent of our 200 largest corporations were controlled by a group of individuals owning half or more of the stock of the companies<sup>9</sup> Again, a survey of some 4000 companies in 1925 discovered that the directors and officers of the companies owned only 10.7 per cent of the common stock and 5.8 per cent of the preferred

<sup>8</sup> United States Department of Commerce, Bureau of Foreign and Domestic Commerce, *Survey of Current Business*, November, 1947, pp 16, 17

<sup>9</sup> A A Berle, Jr., and G C Means, *The Modern Corporation and Private Property* New York The Macmillan Company, 1938, p 122 *et seq*

stock.<sup>10</sup> These statistics suggest the importance of corporations as owners of productive wealth in the United States and the extent to which corporations are controlled by relatively small numbers of individuals who do not own large portions of the businesses which they control.

In this situation, the ordinary stockholders of corporations are in the nature of absentee owners, who may buy and sell their shares without affecting the actual operation of the business. They do not directly own the underlying corporate wealth, have little control over it, and have almost no responsibility to the general public for the way in which it is operated. Their investments have high or low values as the result of the activities of other individuals who are largely beyond their control. On the other hand, the actual managers of corporate wealth are employed on a salary basis, but often receive large bonuses or shares in the profits. Not infrequently, they have been able to secure additional gains by taking advantage of inside information, by manipulating the securities of their companies, and by getting their companies to make purchases from other corporations in which the managers were financially interested. Thus, in the modern corporation we have, in many cases, both the maximum separation of ownership from control and the divorce of private rights from responsibilities to the public. It is not surprising that many of the worst abuses of wealth have occurred within the domain of corporate property.

*Freedom of Enterprise.* Freedom of enterprise is another basic institution of a capitalistic economic system. It refers to the general right, which each individual has, to engage in any line of economic activity which appears desirable to him. He is not compelled, as many people were in more ancient times, to follow such economic activities as seemed desirable to the lord of the manor, or some other superior economic being, and he does not have to become a grocer or furniture manufacturer because his father is established in the one or the other of these types of enterprise. As far as the government is concerned, the individual is free to move to any part of the country, select any occupation which pleases him as his own, and found and operate a business unit in virtually any field of economic activity. By comparing market indicators known as prices and costs, he is supposedly able to select a field of activity which promises to be

<sup>10</sup> Federal Trade Commission, *National Wealth and Income*. Washington Government Printing Office, 1926, p. 159.

remunerative, the institution of private property furnishes the social sanctions necessary for the use and control of the productive agents necessary to his business, once he has chosen it on the basis of freedom of enterprise, and freedom of contract and the price system afford an opportunity to secure funds and gather together the required productive agents. Thus, the various institutions of capitalism, with competition as a sort of overall governor and regulator, are supposed to work together for the successful carrying on of the processes of production and exchange.

The institution of freedom of enterprise is not so old as some capitalistic institutions, such as private property, and no one attempts to justify it on the basis of labor or natural rights. The theory which is ordinarily used to explain and justify the existence of freedom of enterprise is quite simply one of social welfare. That is, the individual, in choosing the field of economic activity in which he will be most productive and useful to himself from the point of view of private profit, will also be selecting the field, it is assumed, in which he will be most productive and useful from the point of view of group welfare. The theory does not assume any high degree of altruism or desire for social service on the part of the individual. Indeed, he may be perfectly selfish and may choose his field of activity purely on the basis of the prospect of getting the greatest possible income for himself, but the result of his activities will be usually the greatest possible contribution which he can make to the production, income, and welfare of society as a whole.

*Restrictions on Freedom of Enterprise.* The social-welfare theory in connection with freedom of enterprise, like the similar theory in support of private property, assumes that social welfare will be maximized if we can induce each individual to produce commodities or services which will have the greatest possible value on the market. This assumption, as we shall see later, is by no means always justified. Quite apart from this objection, however, capitalistic societies have never been willing to extend complete freedom of enterprise to the individual. That is, it has always been recognized that the individual, in selecting the field of activity which would be most profitable for himself, might well choose something which would be, clearly and by common consent, anti-social. In such cases, governmental units under capitalism have not hesitated to step in with prohibitions or restrictions.

Thus, individuals are forbidden outright to steal, commit burg-

lary, organize murder for profit, operate houses of prostitution, or peddle drugs. In some cases, as under the prohibition of the manufacture and sale of alcoholic beverages, they are forbidden to carry on activities which were formerly regarded as quite legitimate. Patent and copyright laws are intended to keep people from misappropriating the writings, musical compositions, or inventions of others and selling them for their own profit. In other cases, restrictions on entry into certain types of business are substituted for outright prohibitions. People are not allowed to function as doctors, lawyers, or certified public accountants unless they have completed extensive courses of training to prepare them for the work and have been able to demonstrate their ability to carry on the occupations by passing rigorous examinations. People who wish to operate such establishments as taverns, hotels, and barber shops are frequently required to take out licenses and pay considerable license fees. In some such cases, the license and fee may be intended to limit the number of such enterprises which will operate within a certain area, and they are usually intended to insure that the operators will meet certain minimum conditions or requirements which are imposed in the interests of the public.

Even after setting up a productive enterprise in a certain field, the individual may find himself subject to a host of additional regulations which indicate what he should or should not do in carrying on his business. However, these latter regulations, as exemplified in the fields of banking, transportation, public utilities, and even agriculture, are not really restrictions on freedom of enterprise so long as they only regulate going concerns in the various industries and do not restrict freedom of entry into the industries, though they may often have both effects. In any case, we should note that the restrictions on freedom of enterprise ordinarily apply to all persons who wish to enter the fields of activity in question and are not intended to give some persons differential advantages over others. Even with all the restrictions, the individual is much more free than he would be in a system in which his choice of activity would be controlled by such matters as race, religion, or social class. The restrictions on freedom of enterprise under capitalism are merely exceptions to the rule, and not the rule itself. They are departures from the norm.

*Freedom of Enterprise and Modern Capitalism.* In a well-developed capitalistic system, the institution of freedom of enterprise

does not mean as much as it did many years ago. It merely gives the individual freedom from certain types of restraint in founding an enterprise or choosing an occupation. It does not guarantee him the economic ability to do what he wishes in these matters. Modern productive technology often indicates the desirability, from the point of view of increasing efficiency and minimizing money costs, of using large-scale productive units in industry. The modern corporation, with its great ability to raise capital funds, furnishes a vehicle for the achievement of such large scale units. Under these conditions, many industries are operated by a comparatively few large-scale and well established firms. The individual just starting out in economic life may be perfectly free, as far as legal and political restraints go, to enter automobile production or steel manufacture and set up a new concern in competition with those already present in these industries. At the same time it may be economically impossible for him to start an enterprise which will be able to compete effectively with the industrial giants now operating in these fields. In many industries the modern corporation has done much to change the significance, if not the nature, of the right of freedom of enterprise for the individual, though in other fields of production it is still feasible economically for the individual to start a new enterprise.

Thus, for many persons and in many industries, freedom of enterprise means economically only the right to choose an occupation rather than that of establishing an enterprise. And even in choosing an occupation, there are economic limitations in the midst of legal freedom, for the individual must furnish his own equipment. He may be restricted in his choice by his own lack of native ability, his inability to obtain the necessary training, or his lack of desirable social and business connections. Both in founding an enterprise and in selecting an occupation, freedom of enterprise is not the same thing as equality of opportunity.

**Economic Motivation** Economic motivation is a third important institution of capitalistic systems. Economic motivation differs from the other institutions which we have discussed inasmuch as it refers merely to a customary or habitual way of reacting in various economic situations and is not surrounded, as is, for example, private property, by large numbers of legal sanctions. It means that individuals under capitalism are usually motivated by the desire for economic or pecuniary gain in their economic activities. That is,

individuals attempt to follow their economic self-interest and try to get as many economic goods as possible for themselves, or for persons closely associated with themselves, without much regard for the effect of their actions on other people. The desire for economic gain is supposed to make people work harder and longer than any other motive which could be substituted for it.

The existence of economic motivation for people under capitalism should not be taken to mean that every individual in the system is completely absorbed in efforts to obtain the largest possible quantities of economic goods for himself with a minimum of disutility or effort. The famous "economic man," who not only seeks but succeeds in obtaining maximum income at minimum cost, is a figment of the imagination. Many other factors besides a mere selfish desire for pecuniary gain influence individuals even under capitalism. They seek to acquire power, they desire prestige and the admiration and respect of their particular social group or of people in general, and they are driven by the pleasure or satisfaction which they find in their work itself, by the desire to serve society as a whole, and by family affections. To be sure, many people, who are motivated by such factors as the desire for prestige or power, pursue pecuniary gain as relentlessly as if it were the final goal of their activities rather than just a means to an end. In other cases, individuals may give up opportunities for large incomes in order to remain in occupations which they find pleasant or satisfying, may reject better paying positions in distant localities in order to remain in familiar places near the other members of their families, or may satisfy a desire for social service and security by remaining in governmental positions at comparatively modest salaries when they might obtain greater pecuniary rewards in private business. However, we should note that some writers regard all these other factors as part of economic motivation rather than as outside factors which lead to exceptions from the general principle.

**Economic Motivation and the Profit Motive** Economic motivation is frequently confused with what is called the profit motive. The two things are closely related, for the profit motive is a part of economic motivation, but the terms should not be used interchangeably. The desire for "profits," as such, is limited in its influence to individuals who are in a position to make profits as a distinctive type of economic return, that is, to individuals who are business enterprisers and assume ultimate responsibility for the conduct of

business enterprises. Economic motivation, however, could continue to function even in an economic system in which the government owned and operated all industries, and opportunities for private profit were entirely eliminated. That is, considerable differences in wages could prevail between occupations and special prizes could be given for unusual accomplishments, and the citizens as workers could strive mightily to qualify for the better paying occupations and for the special rewards. Economic motivation as a whole is clearly much broader than the profit motive.

*The Source of Economic Motivation.* The question of the source of economic motivation, as a capitalistic institution, has led to a great deal of controversy. Even persons who can see that such institutions as private property and freedom of enterprise are not of natural origin are likely to believe that economic motivation has its source in human nature. According to this point of view, human beings are naturally selfish and acquisitive and will put forth great efforts in economic activity only when there are prospects of economic gain as a result. Capitalistic systems which stress acquisitiveness as a human characteristic have developed because of the presence of this attribute in human nature and such systems are more likely to be efficient, productive, and progressive than any other systems because they are well adapted to man's natural tendencies. If economic motivation, or acquisitiveness, is a fundamental part of human nature, it presumably cannot be changed by altering the economic, social, and political system, and non capitalistic systems, which attempt to eliminate or play down economic rewards as a source of motivation for the individual citizens, are to that extent doomed from the outset.

Since so many economic institutions can hardly be considered to be of natural origin, many people are suspicious of this explanation of the source of economic motivation. They believe that human beings behave acquisitively under capitalism because this system stresses acquisitiveness and bestows its greatest rewards on those individuals who behave in this way. In the presence of dangerous enemies, the members of an animal species which enjoy a high degree of protective coloration are more likely to survive than those whose coats are, for some reason, of different hues. Similarly, acquisitiveness is an attribute necessary for the success, if not for the survival, of individuals in a capitalistic system. If acquisitiveness is largely an acquired characteristic under capitalism

and is not deeply rooted in human nature, it may be possible for non-capitalistic economic systems to induce people to work hard, aspire to difficult and responsible positions, and produce inventions, even though large differential economic rewards are not offered for those activities. In other words, other sources of motivation could be used to replace the economic or pecuniary. With people accustomed to behaving acquisitively under capitalism, such a change could not be made overnight, but it could be brought about eventually according to this point of view. We cannot pursue this controversy further at present, but it will come up again in later sections of our study.

In so far as economic activities are carried on by corporations under modern capitalism, the economic character of motivation is clear. Private individuals, whether or not they are corporate stock-holders, may be motivated in part by many other considerations besides the desire for economic gain, but most corporations, as artificial persons or impersonal beings, pursue profits with great if not utter abandon. In their never-ending search for economic gain, they approximate, as closely as anything can in modern life, the classical concept of the "economic man."

Whatever the origin of economic motivation may be, its existence as a capitalistic institution is most often justified in terms of social welfare. The desire for economic gain is supposed to make individuals behave economically and to induce them to make the scarce agents of production go as far as possible in the increasing of production, the satisfaction of human wants, and, according to this point of view, the enhancement of the social welfare. The individual, though motivated only by a selfish desire for gain, is led to accomplish an end which was no part of his intention—the conferring of a benefit on society as a whole. He seeks to increase his productiveness only in order to obtain a large personal income, but the result is the placing of the greatest possible quantity of goods at the disposal of society as a whole.

It is obvious that there are many cases even under modern capitalism in which this unanimity of private and social interests actually exists. In other cases, individuals may seek to maximize private gains by forming monopolies and restricting production, by adulterating foods and other products, by producing and selling noxious patent medicines and drugs, or by employing their workers for long hours, at low wages, and under miserable working conditions. When

the desire for private gain leads individuals to activities which are anti-social, society as a whole, through its government, may not hesitate to step in with restrictions and prohibitions even under capitalism. Such restrictions and prohibitions ordinarily affect freedom of enterprise and the rights of private property directly, but indirectly they curb the ability of the individual to follow his desire for economic gain.

*The Price System* Given the institutions of private property, freedom of enterprise, and economic motivation, individuals under capitalism are supposed to make most types of economic decisions on the basis of prices, price relationships, and price changes. The price system is such an important institution of capitalism, and attempts to modify its operation or eliminate it entirely under other systems present such interesting problems that we shall leave the full discussion of it to later chapters on the making of economic decisions under capitalism and other systems. For the present, we shall merely point out that decisions as to the kinds and quantities of economic goods to be produced, as to the allocation and distribution of existing supplies of land, labor, and capital among the various industries and enterprises of the system, and as to the parts of the national money income which should be devoted to current consumption on the one hand, and to saving, investment, and capital formation on the other, are supposed to be made primarily on the basis of price relationships under capitalism, while price movements are supposed to adjust the quantities of economic goods which buyers are willing to purchase to the quantities of these goods which are available for the market. Such a widespread dependence upon prices implies that a capitalistic economic system must be a money economy, and in all probability a credit economy as well.

*Competition* The attempts of individuals to further their economic self-interest, under the protection of the institutions of private property and freedom of enterprise and with the guidance furnished by the price system, result in competition, which is another basic institution of a capitalistic economy. Like economic motivation, competition is a way of reacting in economic situations, it is a complex pattern of human behavior. Competition, in the strict sense of the term, exists in the market for a given economic good or productive factor only if several general conditions are fulfilled. In the first place, there must be a large number of both buyers and sellers in the market. The number of buyers and sellers

is considered large if any one buyer or seller is substantially powerless to affect the price of the good or productive factor by his activities. This means that the demand for the product of any one seller or for any one supplier's stock of a productive factor is perfectly elastic, that is, he can offer more or less of his product or factor without affecting the price per unit which he receives. On the other side of the market, the supply of the product or productive factor is perfectly elastic to any one demander so that he may increase or decrease his purchases of the good or factor without affecting the price per unit which he must pay. In the second place, the individual sellers and buyers must be independent. There must be no conspiracies or agreements among buyers or among sellers with regard to production, sales, purchases, or prices. Both sellers and buyers are supposed to be reasonably intelligent, and reasonably well informed concerning market conditions affecting the economic good or productive factor. Factors of production are supposed to be mobile as between industries and occupations and, where possible, between places. Finally, the prices of economic goods and productive factors are supposed to be determined by the joint action of the forces of demand and supply without governmental interference.

Clearly, competition in the economic sense is not a natural thing. It is a social pattern produced by the operation of the various supporting capitalistic institutions. Its justification, like that of other capitalistic institutions, is found in the notion that it contributes to the social welfare. When the industries and markets of an economy are organized competitively, certain supposedly desirable results are forthcoming. First, competition is supposed to bring efficiency in the operation of industry and business by granting economic success to those enterprises which are efficiently operated and by relentlessly eliminating those which are inefficiently and wastefully operated. Thus, each enterprise which would survive must make use of the best machines and productive methods available and eliminate waste at all points in its organization, while the removal of inefficient producers from the market tends to leave productive factors in the hands of those enterprisers who can use the factors most effectively. Again, competition is supposed to lead to innovation and technological progress. Better productive methods or machines which increase efficiency and lower cost, or new qualities or superior performance of an economic good which enable it

to satisfy a human want more effectively than the products of other enterprisers, give certain enterprises a greatly prized differential advantage over others with respect to income. But such differential advantages are wiped out sooner or later in a competitive industry and the continuing result is a tendency for consumers to be able to obtain better and better products at lower and lower prices.

Finally, competition is said to be a regulator of economic activity, a means whereby the productive efforts of numerous individual enterprisers are correlated with the desires of consumers as expressed on the market through prices. Success in competition depends on the ability to give consumers the right amount, quality, and kinds of goods. Enterprisers who supply goods which are not suited to consumers' desires, which are of unsatisfactory quality, or which cost more than the similar products of other enterprisers, tend to fall by the wayside. If the total output of an economic good is small relative to the effective demand on the market, the existence of a profitable price will furnish the stimulus for a competitive industry to expand production, and, if necessary, plant facilities. On the other hand, if competitive producers turn out a total output which is large relative to effective demand on the market, unprofitable operation will tend to force some competitors from the industry and bring about a more suitable adjustment of output to effective demand. The competition of other buyers keeps the individual buyer from obtaining economic goods at prices as low as he would like, while the competition of other sellers makes it impossible for the individual seller to charge as high a price as he would like to get for an economic good. Thus, competition is supposed to work in conjunction with the other capitalistic institutions to achieve the maximum production at minimum cost of precisely those goods which consumers most desire, in so far as the relative strength of consumers' desires is accurately indicated by the prices which prevail for various economic goods on the market. And under capitalism these results are often taken to mean the achievement of social welfare.

Critics of capitalism are generally unwilling to accept this account of the merits and advantages of competition, for they believe that, as it operates in practice, competition produces several wasteful results and tendencies. Competitive producers wish to be able to handle not only their usual volume of business but also any cus-

tomers they may be able to maneuver away from their competitors, and the result, from the point of view of the economy as a whole, is idle productive capacity and duplication of productive facilities in many industries. The desire to obtain a differential advantage over other producers leads enterprisers under competition to produce a wasteful and excessive number of styles, shapes, sizes, and colors of economic goods. Much of our large volume of competitive advertising is considered by these critics to be totally useless from a social point of view, and the competitive exploitation of natural resources is notoriously wasteful and inefficient. We shall have occasion to investigate these claims in detail in Chapter 22.

*Modifications of Competition.* Whatever the merits and demerits of competition may be, the fact is that many of the industries and markets of an advanced capitalistic system, such as the United States, are not organized on the basis of competition, in the strict sense in which we have defined the term. The governments of capitalistic economies place many restrictions and limitations on economic activity, and interferences with competition are the result. Consumers are not left to depend entirely on the tender mercies of competition to furnish them with foods and drugs of acceptable purity and quality, for there are laws which provide certain standards in these matters. Again, laws which provide minimum wages and maximum hours for workers in many industries may seriously alter the results which the ordinary operation of the labor market would produce. In some cases, governments may actually prohibit the operation of competition in certain fields of economic activity, as, for example, when a governmental unit grants to a public utility enterprise the exclusive right to sell a certain commodity or service in a given market area. Governmental activities which interfere with competition usually modify the rights involved in freedom of enterprise and private property as well, so we see that governmental prohibitions and restrictions ordinarily affect the operation of several institutions at once instead of affecting just a single institution.

Even when the government does not intervene in economic activities, one or more of the other market conditions necessary to competition in the strict sense may not be present. The processes of production in manufacturing are usually so highly technical that consumers of the products have no chance to be well informed concerning the quality of the goods which they buy. In choosing

among the many brands or varieties of goods which are available for the satisfaction of a certain general want, consumers are often forced to select one variety or another at random, or rely upon the advertising claims which manufacturers make in "puffing" their wares In similar fashion, the workers in a labor market may be very poorly informed concerning the various opportunities which are available for their employment, and they may be unable to move from one occupation to another, or from one place to another, even if they know that jobs are open that are superior to those which they already hold

Many capitalistic industries are owned and operated by a relatively few large firms, instead of the many small firms which strict competitive conditions require In some cases, a single large firm will control all or a large part of the productive capacity of an industry, or a few large firms will act in close harmony to achieve monopolistic control Even when the few large firms in an industry enter into no formal agreement or combination, they usually cannot be as independent of each other as competitive conditions would necessitate In addition to cases of outright monopoly and quasi-monopoly, many industries operate under conditions of monopolistic competition The firms in these industries turn out products of the same general family or type, but not identical goods They "differentiate" their products on the basis of mechanical features and gadgets, brands, packages, and other devices, and attempt to convince customers of the superiority of their particular products through extensive advertising and salesmanship Although it cannot be said that the firms under monopolistic competition do not compete with each other at all, there is very seldom anything resembling price competition between them, for a price cut by one producer would usually be matched quickly by similar reductions on the part of other producers, and no one would gain by attempting to undersell others Thus, no matter which company's brand of cement, gasoline, or cigarettes one buys, the price is the same for all brands that are on the same general level of quality

The extent of non competitive conditions in American industries is much greater than many people suppose According to a recent report, "one company in each field controls all, or nearly all, of the nation's supply of aluminum, nickel, molybdenum, magnesium, shoe machinery, glass container machinery, and scientific precision glass, provides nearly all of the domestic telephone service . and

operates all of the sleeping and parlor cars "<sup>11</sup> In other cases, as in the domestic telegraph service, the importation of bananas, the production of plate glass, the production of glass bulbs, glass tubing, and rod for electric lamps, the production of electric accounting machines, the manufacture of railroad air brakes, the production of compressed oxygen and acetylene, and sulphur production, "pans" of firms control all or nearly all of the supply of certain economic goods<sup>12</sup>

Non-competitive conditions exist frequently also in industries in which no single firm or pair of firms controls all or almost all of the output. Of the 1807 products studied from among those included in the Census of Manufactures for 1937, there were 291 in which the most important single firm controlled between 50 and 75 per cent of the total supply. In the case of 37 products, four firms accounted for the entire supply, in 164 cases, four firms turned out over 90 per cent of the supply, and in 328 other cases the part produced by the four leading firms was not revealed (in order to prevent the identification of individual firms). There were 670 products in which the four leading firms produced 75 per cent or more of the supply, or in which information on this point had to be withheld. The general conclusion was that from two-fifths to one half of the goods studied were produced in fields in which four concerns controlled 75 per cent or more of the supply.<sup>13</sup> Non-competitive conditions often result from price leadership, price agreements, basing-point systems, patent pools, market sharing, interlocking directorates or financial interests, and trade association activities.

Though comparatively few of our American industries operate under strict competitive conditions, we should not jump to the conclusion that our economy is not competitive at all. Monopolistic competitors in an industry compete with each other for customers on the basis of quality and product differentiation. They compete for customers with the enterprisers of other industries which produce other families of products intended for the satisfaction of the same general want on the part of consumers, as, for example, the monopolistic competitors in the manufacture of electric refrigerators compete with the manufacturers of the old-style ice refrigerators.

<sup>11</sup> Temporary National Economic Committee, Monograph No 21, *Competition and Monopoly in American Industry*, Washington Government Printing Office, 1940, p. 69.

<sup>12</sup> *Ibid.*, pp. 98-110.

<sup>13</sup> *Ibid.*, pp. 113-118.

They compete with enterprisers in completely unrelated industries for the limited incomes of consumers in general Monopolistic competitors in any industry compete with each other, and with enterprisers in all other industries, for supplies of the scarce agents of production The firms in any given industry compete on the basis of technology That is, they continually try to develop improved machines and methods of production which will both lower their own costs of production and render obsolete the machines and methods of competitors Even monopolists, who do not have to face competition within their own industries, must compete with enterprisers in other industries for the limited money incomes of consumers and for supplies of the scarce agents of production Finally, some of our industries operate under conditions which approximate competition in the strictest sense of the term Thus, a modern capitalistic economic system is said to be competitive in the sense that it is more nearly competitive than anything else Just as the existence of economic motivation in a capitalistic economy does not mean that all individuals are always and completely motivated by the desire for economic gain, so the existence of competition in the same system does not require the existence of *perfect* competition in all fields of economic activity

***Capitalistic Institutions in Wartime*** A period of great emergency, such as that brought about by participation in a major war, may result in serious modifications of the economic institutions of capitalism on at least a temporary basis During World War II, for example, the federal government of the United States controlled production to a great extent, increasing production sharply in some fields, retarding or even eliminating it in others, permitting or encouraging the entrance of new firms in some industries, and excluding them from others The government controlled the allocation of capital funds, machinery and equipment, materials, and even labor, among the industries and businesses of the country Wages, rents, interest rates, and profits were controlled, as were the prices of a multitude of finished commodities and services Imports and exports were closely regulated, the allocation of many finished commodities among consumers was subjected to rationing on the basis of physical quantities, and heavy wartime taxes severely modified the distribution of the national income, with some important effects upon incentives As a result, our traditionally capitalistic system

came to resemble, in many economic respects, the fascist systems against which we were struggling

### *Economic Institutions under Socialism*

**Private Property** Under ideal socialism, so its proponents say, the rights of private property would be limited to consumption goods, since productive wealth (land and capital) would in general be owned by society as a whole. However, some socialists say that the social ownership of the means of production would be limited to the land and capital used in "large-scale production." That is, aggregations of land and capital which were so large as to require the use of hired labor in their operation would have to be socially owned, but small amounts of land and capital, which could be operated in production by the owner (and perhaps other members of his family) and which would not involve employer-employee relationships, wage slavery, and exploitation, could perhaps be safely left in the hands of private owners. Sometimes it is even contended that certain industries, which operate fairly satisfactorily under private ownership and which are not well suited to governmental ownership and operation, might well be left in the hands of individual owners or cooperative groups. These modifications would apparently permit private individuals to own and operate small farms, stores and repair shops, and shops for handicraft production even under socialism, and it is possible that certain fields of economic activity, such as agriculture and retail merchandising, might be carried on entirely by private owners or cooperatives. However, the general conclusion is that the great bulk of land and capital would be owned by society as a whole under socialism.

In the socialistic economy of Soviet Russia, the material means of production are owned almost completely by society as a whole. Even by the end of the Second Five-Year Plan (1937), some 98.7 per cent of the land and capital of the system had been brought into socialized or collective ownership.<sup>14</sup> The land of the country was nationalized as of February, 1918, and is completely owned by society as a whole, while practically all capital goods in manufacturing, and the heavy capital goods in other fields of activity, are similarly owned. The numerous collective or cooperative farms of

<sup>14</sup> M. T. Florynsky, *Toward an Understanding of the USSR*. New York: The Macmillan Company, 1939, p. 173.

the system own farm buildings, draft animals and other livestock, some machinery, and stocks of seed, and have the right of "perpetual use" of their land, though tractors, combines, and other types of heavy agricultural machinery are owned by the state and are furnished to the collective farms on a kind of rental basis. The fairly numerous marketing cooperatives and producers' cooperatives in handicraft production own certain limited quantities of capital goods, and very small amounts of capital are in the hands of individual peasant farmers and handicraft producers.

*Freedom of Enterprise.* Under ideal socialism, the people as a whole, through various units of government, would operate, as well as own, the productive wealth of the country. This does not mean that the central government of the system would own and operate all industries, for many types of production might be allocated to other governmental units, but it does mean that freedom of enterprise would exist only for governmental units as representatives of the people as a whole. With rare exceptions, private individuals could not be business enterprisers or receive profits as private income. On the other hand, the individual workers of the system would continue to enjoy considerable freedom of occupational choice under socialism.

This description is substantially applicable to the socialistic economy of Soviet Russia. Most important types of economic activity are operated, as well as owned, by the federal, republic, district, or local governments. However, just before the outbreak of World War II, the roughly 250,000 collective or cooperative farms cultivated over 90 per cent of the land which was in use, and included some 18.8 million peasant households, or 93.5 per cent of the total.<sup>15</sup> There were also a little over a million small independent peasant farms. In 1947, after various new areas had been added to the territory of Soviet Russia, there were said to be 220,000 collective farms, and several million individual peasant farms.<sup>16</sup> A few million persons are members of various cooperative enterprises in handicraft and service production, and many thousands of consumer cooperative organizations operate retail stores and are served by cooperative wholesaling organizations. In addition, there are numerous but relatively unimportant private enterprises in handicraft production,

<sup>15</sup> *Ibid.*, p. 200.

<sup>16</sup> Harry Schwartz, *Russia's Postwar Economy*. Syracuse: Syracuse University Press, 1947, p. 54.

and service trades. However, the private and cooperative enterprises in Soviet Russia do not really enjoy freedom of enterprise in the capitalistic sense, for their activities are covered by the economic plans of the country and their operation is quite rigidly controlled by means of prices, taxes, interest rates, rentals, and other factors which are directly under governmental jurisdiction. Freedom of enterprise really exists only for society as a whole, though Russian workers ordinarily have a large degree of freedom in choosing their occupations.

**Economic Motivation** An ideal socialistic economy would rely on economic motivation to some extent, but the significance of this institution would be much less than under capitalism. The profit motive itself would be virtually eliminated, since private individuals in general would not be allowed to own and operate enterprises for private gain. Since productive wealth would be owned very largely by governmental units, as representatives of the people, individuals would not be motivated by a desire to accumulate land and capital in order to receive rent or interest as private income. Most individuals would work for some governmental unit or other and would receive only wages as income. This is where economic motivation comes in, for most socialists would permit moderate differentials in wages as between different industries and occupations, though there are a few socialists who hold out for a strictly equal distribution of income. By moderate differentials in wages, socialists presumably mean that the highest wage paid to anyone would be not more than 10 to 15 times the lowest wage paid to anyone. Such differentials are large in comparison with perfect equality, but are very modest in comparison with the differences in individual incomes which prevail under capitalism. With the private ownership of wealth limited to consumers' goods and with inheritance severely restricted, if permitted at all, inequalities in the distribution of wealth should be very small under socialism as compared with capitalism.

Though economic motivation would be retained to some extent under socialism, such a society would attempt to emphasize other types of motivation. Altruism would replace the desire for economic gain to a considerable extent. Individuals would be supposed to work for the good of society as a whole, for prestige (or the esteem and admiration of their fellow men), or to obtain positions of power in the economic system. Under capitalism, prestige and power are often sought indirectly through obtaining a large income and ac-

cumulating wealth, but under socialism they would be separated rather thoroughly from the seeking of economic gain Public honors would be available for unusual accomplishments in production, and security against unemployment, old age, and other economic misfortunes might serve as a spur to productive effort Underlying everything else, of course, would be the public power of compulsion, with penalties for unsatisfactory efforts and results on the part of individuals, and the ultimate requirement that every able person must work if he wishes to eat

Since it will be necessary to deal with the question of incentives in Soviet Russia in detailed fashion later in our discussion, we propose to limit the present treatment severely and merely indicate that the Soviet Russian economy lives up to the socialistic model in a general way While the profit motive as such is almost completely eliminated in Soviet Russia, economic motivation is relied upon to a considerable extent and there are fair-sized differentials in money wages In 1938, for example, maximum differentials in money wages were fixed by law in certain industries In industry and transportation the lowest rate of pay was set at 110 rubles per month and the highest rate at 2000 rubles per month These rates of wages produced a differential of a little over 18 to 1 from top to bottom Of course, it is possible that the lowest paid workers in other fields received less than 110 rubles per month and there were probably other positions in the economy which paid more than 2000 rubles per month During the war and postwar period, in the face of the necessity of giving all classes of workers maximum incentives to increase production, there was some broadening of differentials in wages and salaries Besides money wages, the individuals of the Russian system receive part of their real income from the government in the form of direct grants of commodities and services, and these grants may increase, decrease, or merely maintain the differentials which exist on the basis of money wages, according to the manner in which they are distributed among the workers with different levels of money income

The Soviet Russian economy also relies to some extent on other motives, such as altruism, enthusiasm for socialism and economic planning, and socialist competition, or the efforts of the workers of various socialized enterprises to outdo each other in the matter of increasing production A considerable range of public honors is available for conspicuous achievements in production, and some of

these honors carry certain economic rewards with them as well. Some economic positions afford much more prestige and power than others, and security against unemployment, old age, and other economic ills is given. Many penalties are also provided for workers whose attitudes, efforts, or results are particularly unsatisfactory and the public power of compulsion can be used as a last resort to get the workers to function in the manner and places desired by the planners.

**The Price System** According to most socialists, the ideal socialistic system would retain money and the price system, but it would not rely on price movements and price relationships in making important economic decisions to nearly so great an extent as does a capitalistic economy. Decisions as to the kinds and quantities of goods to be produced, as to the allocation of land and capital among the various enterprises and industries, and as to the relative proportions of the national real income which should take the form of capital goods and consumers' goods, respectively, would be made by some governmental agency or other on the basis of economic planning rather than on the basis of price indicators. On the other hand, price relationships might be relied upon for the most part to effect the distribution of workers among industries and occupations and to bring the market demands and supplies of various economic goods into balance. Thus, the price system would be replaced to a great extent by the institution of economic planning as the prime mover of the economic system. This is, as we shall see, substantially the situation which exists in the socialistic economy of Soviet Russia.

**Competition** A great reduction in the importance of competition in economic life is one of the features of an ideal socialistic system. Individual workers would presumably compete to get into the better paying and more pleasant occupations of the system, and consumers would compete for the available limited supplies of various consumers' goods and services since the socialistic intention is to give consumers considerable freedom of choice in spending their money incomes, but that is all. In other respects, the governing influence of competition would be replaced by the dictates of economic planning. This is the situation which exists in Soviet Russia if we add to the types of competition just mentioned the "socialist competition" to which we referred in another connection and some unauthorized competition of enterprises and industries to secure supplies.

of materials, fixed capital goods, or labor A socialistic economy is in general intended to be a single great cooperative enterprise

### *Economic Institutions under Partial Socialism in Britain*

Since the Labor Party took over the reins of government in July, 1945, Great Britain has been moving in the direction of "partial socialization" of her economic system Through the first half of 1949, seven important industries (coal, banking, telecommunications, civil aviation, inland transport, electricity and gas and coke) had been nationalized and brought under public ownership and operation and the nationalization of one other (steel production) seemed imminent However, the objective of the Labor Government is said not to be complete socialization, for it is said that, when all proposed nationalization measures have been carried out, about 20 per cent of industry will be publicly owned and operated, while 80 per cent will be left to private ownership and free enterprise<sup>17</sup>

The nationalization process has an obvious impact on the institution of private property, the extent to which Businessmen enjoy freedom of enterprise, the pervasiveness of competition in the economy, and the operation of the price system Actually, however, governmental control over the economic life of the country and the modification of capitalistic institutions have gone forward much more rapidly than the bare nationalization program itself would suggest Rationing by physical quantities applies to a certain number of scarce commodities Almost all prices are strictly controlled Rents are being kept at prewar levels and the government's housing program emphasizes low rentals made possible by subsidies Imports and exports are almost completely under license, and foreign exchange is controlled Enterprisers face many limitations on what they can produce Many industries not directly involved in the nationalization program are subjected to strict governmental control through almost countless regulations

Inefficient managers in manufacturing and agriculture can be displaced and government nominees substituted The government can see to it that supplies and materials are made available to certain industries and are withheld from others It can divert both public

<sup>17</sup> British Information Services, *Labor and Industry in Britain*, September October 1947, p. 162

and private investments into government approved channels and prevent them from going into others. It can freeze workers in jobs considered essential and direct them to move from certain jobs to others. It has the power to control rates of pay, hours, and working conditions. It can order goods to be exported to certain markets and to be withheld from others. In general, the government has the power to do anything to insure that the whole resources of the community are available for use and are used in a manner best calculated to serve the interests of the community. In this situation it is clear that there is little left of the ordinary family of capitalistic institutions. Some people claim, to be sure, that the rather complete governmental control of the British economy is a product of the postwar economic emergency rather than of the advent of partial socialism, but it remains to be seen whether any partly socialized economy can permit the operation of capitalistic institutions to any significant extent in the non-socialized sector of the economy.

### *Economic Institutions under Communism*

If we sought to understand the differences between socialism and communism by examining the platforms of the Socialist and Communist Parties in the United States, we might reach the conclusion that these differences are not very striking and significant. However, there are important differences between socialism and communism as ideal theoretical systems. In the first place, communism would go further than socialism in modifying the capitalistic institution of private property. Under communism, consumers' goods as well as land and capital would be owned by society as a whole. Of course, various consumers' goods, such as groceries, clothes, and tooth brushes, must be allowed to pass into private possession in order that consumption may take place, but the basic title even to such things would remain vested in the entire social group. Freedom of enterprise, as a right of individuals, would be completely eliminated under communism. Individuals would presumably remain free to choose their own occupations, but these choices would be made entirely on some other basis than the desire to receive a large money or real income. That is, in an ideal communistic system, economic motivation would be entirely eliminated. Each individual would choose that occupation in which he could be most useful to society as a whole, would produce to the best of his ability and would

receive real income according to his needs, presumably by helping himself to the various economic goods which would exist in plentiful quantities in public storehouses While the distribution of income according to needs would not result in a precisely equal distribution of real income among persons, unless we assume that all persons have equal needs, economic inequality between persons would be almost completely eliminated under communism and any differences in income which existed would not be based on productiveness or choice of occupation

With wage differentials abandoned as a means of distributing labor among industries and occupations, and with exchanges of commodities and services, in the ordinary market sense, eliminated, it would seem that a communistic system would have no use for a system of money and prices Thus, it is commonly said that these things would be abandoned under full communism and that all important economic decisions would be made on some other basis than price movements and relationships If there were no differential wages for which workers could compete, and if all consumers' goods and services were so plentiful that each person could have all he needed, then clearly the last vestiges of competition as a capitalistic institution would be removed under ideal communism Complete social cooperation would be the order of the day From this brief discussion, we can see that the institutions of Soviet Russia are socialistic in character rather than communistic, even though Russia is widely known as a communistic system and its operation as an economic system is well-nigh completely in the control of the so-called Communist Party

### *Economic Institutions of Fascism*

The fascist economies, as typified by Germany and Italy, held that the goal of their system was found in the ends and objectives of the state, or of the nation as an entity separate from the numerous individuals who compose it at any particular time Economic policies were followed or abandoned not for their own sake or because of their effect on individual welfare but according to whether they appeared to be consistent or inconsistent with the general goal of the system Such a system did not need to make any change in the *nominal* character of economic institutions as such It needed merely, by intervention and restriction, to control the operation of

these institutions so that their effect would be to further the aims of the system.

Thus, the differences between capitalism and fascism did not lie in the basic institutions of the systems, for these institutions were nominally the same in both systems. Under fascism, we saw no such complete concentration of productive wealth in public hands as is presupposed by a system of socialism or communism. The various governmental units under fascism did own and operate some industries, but the great bulk of productive wealth was left in private hands. However, the private owners of productive wealth were not supposed to think that they had any sacred property rights, for they held their wealth only on the sufferance of the "leader," Herr Hitler or Signor Mussolini. The uses which could be made of productive wealth were closely controlled, and private wealth was even expropriated on occasion. Thus, when the government or party found itself short of funds, examiners could be sent to go over the books of private concerns for many years past, and fines of millions of marks or lire might be levied for any false entries or mistakes in bookkeeping however trivial and insignificant. There were no laws or courts capable of preventing such arbitrary governmental actions, or of interfering with the capital levies which were placed on land owners or enterprisers on other occasions.

On paper, the fascist systems made much of such things as individual initiative, economic motivation, and freedom of enterprise as devices for securing the efficient operation of their economies. Unless and until he was interfered with, the individual was free to be a business enterpriser, produce any commodity or service which he liked in any quantity which seemed most appropriate, hire and fire labor, secure supplies of other productive agents on as good terms as he could get, make as much money as he could, and spend or save his income as he desired. Under these conditions, it seemed that the operation of the economic system would be highly competitive in character, and private business men appeared to be able to make their various economic decisions on the basis of price movements and relationships.

Actually, interference with the private operation of business and industry existed to an almost unbelievable extent under fascism. The government could and did restrict, or even prohibit altogether, the entry of individuals into certain industries and businesses. The government at times controlled the prices at which commodities

and services could sell or at which labor or other productive factors could be obtained, it regulated the marketing of economic goods, it set up production quotas or hours of operation for plants and enterprises, it rationed raw materials and supplies, it compelled employers to hire and fire workers along party lines without regard for ability, and it controlled the use of foreign exchange, the importation of materials and supplies, and the exportation of finished goods.

Under these conditions, business enterprises could seek profits but, if profits were made, the government decided whether they could be paid out to the owners of the businesses and to what extent, and it could require the enterprises to invest their earnings in the securities of new plants that were being set up for purposes of economic self-sufficiency, or in government bonds. Differentials in wages existed between the various occupations and industries and the workers sometimes had considerable freedom in their choice of occupations, but as time wore on there appeared a tendency to freeze the workers in their jobs and to mold the class structure of society into rigid and semi-permanent castes or groups. In any case, in view of the great levies which fascist governments made against the wages of workers, it is questionable whether there remained any great degree of economic motivation for them.

Fascism, then, appeared to be different from capitalism in that an all-powerful central government, unrestrained by constitutional or other limitations, interfered with and controlled economic and other activities to an enormous degree for the purpose of directing them toward the achievement of whatever goals seemed desirable to the leaders of the party and the government. Fascism had the institutions of capitalism in name only, for it refused to let them operate in the ordinary capitalistic fashion lest they enhance the welfare of the citizens as individuals instead of making for those different and often conflicting goals which were attributed to the semi-mystical state or nation.

#### QUESTIONS

- 1 "It is customary to define various economic systems in terms of their institutions" Illustrate
- 2 What is private property and why is it said to be basic to the operation of a capitalistic economy? How and why is private property restricted even in capitalistic economic systems?

- 3 Explain briefly the various theories which have been developed to explain and justify the existence of the institution of private property
- 4 Distinguish carefully between private property and corporate property
- 5 Can the institution of freedom of enterprise be justified on the basis of social welfare? Discuss
- 6 How important is the institution of freedom of enterprise to the ordinary individual under modern capitalism?
- 7 "Under capitalism, the desire for economic gain makes people work harder and longer than would any other motive which could be substituted for it" Discuss
- 8 "The importance of economic motivation under capitalism is hardly open to question, but the source of this institution is a matter of considerable controversy" Explain
- 9 Outline the several important functions which the institution of competition is supposed to perform in a capitalistic economy
- 10 "Even in capitalistic economic systems, competition is interfered with and limited both by governmental activities and those of private individuals" Explain
- 11 In view of the many cases of monopoly, duopoly, and monopolistic competition which exist, why is our capitalistic economic system still regarded as competitive?
- 12 How and why are the institutions of a capitalistic economy likely to be modified in wartime?
- 13 "Some economic institutions of capitalism would be modified in a socialistic economy while others would be completely eliminated" Show whether you agree
- 14 Discuss the probable fate of each economic institution of capitalism in an economy of modern socialism
- 15 How do the economic institutions of Soviet Russia compare with those of theoretical socialism? Explain
- 16 How and to what extent has the program of partial socialism in Britain resulted in a modification of the economic institutions of the country? Explain
- 17 "The economic institutions of capitalism would be completely eliminated in a communistic system" Explain
- 18 "The economic institutions of the fascist countries were nominally the same as those of capitalism, but in practice the functioning of these institutions was severely modified" Explain

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## CHAPTER 3

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### **G O V E R N M E N T**

In discussing the nature and operation of economic institutions, it was necessary on several occasions to refer to government as a modifying or conditioning force in economic life. We shall investigate now the nature of the governments of capitalistic, socialistic, communistic, and fascist systems before going into the more strictly economic aspects of these systems. Indeed, in non-capitalistic economic systems the activities of government play such an important part in the operation of the economic system that some knowledge of their governments is essential to an understanding of their economic life.

#### *The Government under Capitalism*

For the most part, our discussion of government in relation to capitalism will deal with rather general matters. Since capitalistic systems have been able to operate successfully under governments which differ considerably in the details of their organization, there seems to be no particular point in setting up the government of any one country as a model for all capitalistic systems and dealing exhaustively with the details of its organization.

***Capitalism and Democracy*** Perhaps because various non-capitalistic economic systems have so often operated under dictatorial governments, there is a tendency in popular discussion to make capitalism synonymous with democracy, and socialism and fascism with dictatorship. Actually, the government of a capitalistic system does not have to be democratic in the strict sense of the term, which would presumably involve direct and equal participation in the government by all citizens. In a large and heavily populated capitalistic system, it would be impossible for all citizens to participate directly in the government as they might in the old New England

town meeting, and it is very doubtful whether the citizens of a capitalistic economy could participate equally in the government in any case since they differ so much as individuals with respect to such matters as wealth and income, economic opportunities, education, and social status. However, the government of a capitalistic system could scarcely be a dictatorship, for it is difficult to imagine a dictatorial government which would not restrict and control economic life to an extent which would be inconsistent with the operation of capitalistic institutions.

*Capitalism and Laissez-Faire* For many years, the idea persisted that the government of a capitalistic system, however it might be organized, should follow a policy of *laissez-faire* with respect to economic activity. That is, its activities should be limited to the performance of a few general functions for the good of all the citizens, and it should not attempt to control or interfere with the economic activities of private individuals. As Adam Smith wrote many years ago:

All systems, either of preference or restraint, therefore, being thus completely taken away, the obvious and simple system of natural liberty establishes itself of its own accord. Every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest in his own way, and to bring both his industry and capital into competition with those of any other man, or order of men. The sovereign is completely discharged from a duty, in the attempt to perform which he must always be exposed to innumerable delusions, and for the proper performance of which, no human wisdom or knowledge could ever be sufficient, the duty of superintending the industry of private people, and of directing it toward the employment most suitable to the interests of the society. According to the system of natural liberty, the sovereign has only three duties to attend to, three duties of great importance, indeed, but plain and intelligible to common understandings, first, the duty of protecting the society from the violence and invasion of other independent societies, secondly, the duty of protecting, as far as possible, every member of the society from the injustice or oppression of every other member of it, or the duty of establishing an exact administration of justice, and, thirdly, the duty of erecting and maintaining certain public works, and certain public institutions, which it can never be for the interest of any individual, or small number of individuals to erect and maintain, because the profit could never pay the expense to any individual, or small number of individuals, though it may frequently do much more than repay it to a great society.<sup>1</sup>

<sup>1</sup> Adam Smith, *The Wealth of Nations* London T Nelson and Sons, 1891 Book IV, p 286

The implications of the "system of natural liberty" are clear. Each individual is assumed to be a more or less rational being and a better judge of his own interests than any government can be. The interests of individuals are closely identified with those of society as a whole, and the individuals of the system, in relentlessly pursuing their own ends, contribute to the maximization of the social welfare. The institutions of capitalism are both natural and beneficent. It is only necessary for the government to provide a setting or environment in which these institutions can operate in free and untrammeled fashion. This the government can do by carrying on national defense, by maintaining justice, law and order, and by constructing and maintaining roads, bridges, harbors, schools, and other public works and institutions.

*Governmental Regulation under Capitalism* The system of natural liberty was not perfectly suited even to the relatively simple economic conditions of 150 years ago, and, in more modern times, the governments of capitalistic systems have more and more often broken the bonds which the system of natural liberty would have placed upon them. It has been realized that the institutions of capitalism are man-made rather than natural and that the proposition concerning their beneficence is one which at best is valid only in the majority of cases. In the operation of capitalistic economies, economic problems have arisen which have seemed impossible of solution at the hands of private individuals and whose great impact on the lives of millions of individuals has brought a demand for governmental intervention.

As a result, governmental regulation is a fairly common feature of economic life under capitalism. In the United States, for example, the phases of economic life which have come under governmental regulation include transportation by rail, highway, water, and air, communications, public utilities in the more limited sense and public utility holding companies, commercial banking, investment banking, coal production, international trade and foreign exchange, insurance companies, monopolies and trusts, agriculture, collective bargaining and trade union activities of other kinds, the wages, hours, and working conditions of labor, and others. However, under capitalism, governmental regulation is not assumed to be good in and of itself nor is it ordinarily intended to bring about the replacement of the capitalistic system with some other variety of economy. In general, it is intended to prevent or eliminate abuses.

and to enable the actual capitalistic system to operate more nearly like the ideal, theoretical model. The impression is that governmental intervention is an evil which must be tolerated or encouraged only when it seems likely to prevent or remove a greater evil.

In wartime, as we noted in the preceding chapter, the sphere of governmental regulation in an erstwhile capitalistic system tends to be greatly expanded. The government is then likely to undertake to control the kinds and quantities of economic goods to be produced, the allocation of various productive agents among industries and businesses, the apportionment of finished economic goods among consumers, the process of saving and capital formation, and the prices of finished goods and productive agents. Such a degree of governmental control is inconsistent with the operation of a capitalistic economic system. What it means is that the country in question temporarily abandons its capitalistic economy and becomes some sort of planned and controlled economy.

*Governmental Ownership and Operation under Capitalism.* The existence of a capitalistic system does not imply that all fields of economic activity are left exclusively in the hands of private individuals, for some industries, or parts thereof, may be owned and operated by various governmental units. In the various capitalistic systems taken together, governmental units have provided, in whole or in part, such things as transportation, communication, savings bank service, general banking facilities, insurance, educational facilities, harbors, roads, canals, public parks and reservations, botanical and zoological gardens, libraries, art galleries and museums, public baths, tennis courts, golf courses, health service, theaters, water, gas, electricity, hospitals, clinics, medical schools, day nurseries, fire protection, housing, farm products, mineral products, a host of manufactured products, and the drainage, irrigation, and general reclamation of land.

In the United States, governments own and operate productive facilities of many kinds. That is, governmental units of one kind or another own and operate the plants which provide water, gas, and electricity in hundreds or thousands of cities and towns, as well as local transportation systems, markets, airports, beaches and piers, golf courses, ice plants, dairies, laundries, heating plants, coal yards, bridges and tunnels, terminals, warehouses, roads and highways, railroads in Alaska and Panama, radio stations, printing establishments, steamship lines, the post office and postal savings system,

social insurance systems, and carry on projects in connection with reforestation, soil erosion, grade crossing elimination, slum clearance, rural electrification, and rural housing. All this does not mean that governmental ownership and operation is preferred to private in many or most lines of economic activity in our economy. On the contrary, in most fields private ownership and operation is assumed to be better until the contrary can be demonstrated, just as a man on trial in court is assumed to be innocent until he has been proved guilty. The great bulk of our economic activity is still in private hands. However, it is clear that the governments of capitalistic systems do not follow anything like a strict policy of *laissez-faire* today.

### *The Government under Socialism*

**Socialism and Democracy** The question of what the government would be like under an ideal system of modern socialism is an important one. Many socialists would apparently prefer to keep modern capitalism with all its evils rather than to achieve the economic features of socialism in combination with a dictatorial government. That is, modern socialists seem to be in quite general agreement that the government of their system must be a democracy, and that democracy can hardly be achieved under any other system. As one writer says

For short, let us say that Socialism aims at a classless society in which the means to wealth will be communally controlled. It follows that Socialism must aim at Democracy—that is, at assuring to every citizen a real and effective share in the government of his country and of the world. Class equality and communal control mean nothing unless they mean democracy. Class equality is inconsistent with any sort of monopoly or dictatorship in the sphere of government, and communal control means control by all.<sup>2</sup>

And again

We have no right to be disappointed with democracy—much less to yield to our disappointment, for democracy has not yet been tried. It cannot be tried in any real sense until it has been given an environment in which it can have free play. There can be no real political democracy without economic freedom to serve as a foundation for it. There can, indeed, be more or less democratic elements in a society that is undemo-

<sup>2</sup> G D H Cole, *The Simple Case for Socialism*, p 9 Reprinted by permission of Victor Gollancz Ltd., London

cratic in its basic institutions. The democratic elements in a society can be of real value and can serve as instruments for the furtherance of freedom. They are the forerunners of democracy and point the way towards its achievement. But it is nonsense to speak of democracy as actually in being where men are divided into social classes differing grossly in wealth, opportunity, status, education—in short in all those things which make the difference between ruling and being ruled, between the classes for whose sake society is administered and the classes which are doomed to serve as means to other men's ends. Democracy may be in the making, but it is not yet made. In the modern world, there is no real democracy short of socialism.<sup>8</sup>

**Features of Socialistic Government** Modern socialism, then, looks forward to a situation in which the individual citizens would be so nearly alike in economic power that they could participate in the affairs of government with substantial equality. It also envisages a situation in which the national legislature and other governmental agencies will respond freely and accurately to the popular will of an enlightened citizenry. The government will give the people what they want and the citizens will know what they want the government to do on all important matters of public policy, because the citizens will have been subjected to mass education and they will have had an opportunity to hear unbiased presentations of both sides, or all sides, of important questions on which the government must pass. Such an enlightened citizenry is virtually impossible to attain under capitalism, according to the socialists. The various agencies which play an important part in forming public opinion under capitalism, such as the newspapers, for example, seldom, if ever, present all sides of important public questions to the public. They present only the sides of questions and favor the policies which appear to be consistent with their own interests, and try to convince the citizens that their interests are the same as those of the opinion-molding agencies and require the same public policies. And, of course, regardless of the condition of the capitalistic economy as a whole at any particular time, the opinions expressed by these agencies are favorable to the continuation of the capitalistic institutions under which they thrive and prosper. So long as private property exists and the distribution of wealth and income remains highly unequal, most citizens of a capitalistic system are not likely to become as enlightened as the socialists would have them.

It goes without saying that a socialistic democracy would have to

<sup>8</sup> *Ibid.*, p. 26. Reprinted by permission of Victor Gollancz, Ltd., London.

extend the various civil rights, such as freedom of speech, freedom of the press, freedom of assembly, and freedom of religion, to the people, that it would provide free and universal suffrage for adult citizens, and that it would fill governmental offices by election, where possible, so that the officials would be directly responsible to the people. The federal government under socialism would probably not be divided into three more or less watertight compartments, with a system of checks and balances existing between them. The legislature, as the department of government which is likely to be most responsive to the will of the people, would probably be supreme, and its decisions and enactments could not be upset by the other agencies of government. The executive agency or agencies would be, in a sense, subsidiary to the legislature and would hold no veto powers over laws, while the courts would also be secondary in importance and none of them would have any power to declare laws unconstitutional. Thus, the diffusion of responsibility which we now have among the departments of the federal government would be eliminated. There would be no cases in which the legislature would pass laws in response to popular demand, only to see them vetoed by the executive or held unconstitutional by the courts. Under the conditions foreseen by modern socialism, the protection which is now supposed to be afforded by the separation of governmental powers and the system of checks and balances would no longer be needed.

There are considerable differences of opinion among socialists as to the details of governmental organization, as, for example, the question of whether we should have a one-house or two-house legislature. However, it is often proposed that, in some way or other, representation in the legislature should be economic in character. The members should represent industries or occupations rather than states or subdivisions of states. It should be the gentleman from the automobile industry instead of the gentleman from Michigan. Many socialists also seem to think that, in the United States, only the federal and municipal governments would survive under socialism. The present state governments would be replaced by some sort of district governments drawn up along strictly economic lines. Our present states are regarded as historical accidents rather than as economic units and it is frequently true that large numbers of persons in one state will have economic interests which are more like those of citizens of other states than like those of the other citizens.

of the same state. Such a situation is somewhat unfortunate in modern times, for most of the decisions which governments have to make are economic in character. Moreover, there would be no justification under socialism for the many and peculiar local governmental units, other than municipal, which we now have.

*Problems of Socialistic Government* The prospectus which the socialists furnish for their government is interesting, but many problems are involved in their proposals. One problem has to do with the enlightened citizenry. If the various governmental units will deal primarily with economic issues, how can a socialistic system provide mass education and make sure that the citizens understand all sides of the issues? Economic questions, in general, are difficult enough even for college students, and the feat of providing full enlightenment for all the citizens on such matters would certainly be most difficult, if not actually impossible, to accomplish. However, we may concede that it would be possible for the citizens as a whole to be better informed than they are today on the economic issues which are matters of governmental policy, and one might hope that, under socialism, the citizens selected to fill governmental offices would be much better equipped than those of today to cope with the major economic issues which they would face inevitably. Perhaps this is all the socialists really hope for.

There is also some question as to how thoroughly the government of a socialistic system would want its citizens to be enlightened on all sides of important economic issues. The agencies through which information would be passed on to the people would almost certainly be owned and operated by the government, and the government would have official policies in regard to a variety of economic matters which it would desire to have the people favor. Would the government be willing to present full and impartial information concerning possible alternatives to the policies which it is actually following? Would the government press under socialism be expected to present a complete and fair discussion of the merits and demerits of such a matter as, say, a proposed return to capitalism? Would not any citizens who tried to accomplish the same result be likely to have a short and undistinguished journalistic career? The socialists who inhabit a capitalistic economic system usually insist that they should have freedom of speech and of the press in selling their proposed system, but it is far from certain that they would accord

similar rights to persons who desired to oppose the official policies of government under socialism

Even if the citizens are fairly enlightened, there is the question of how responsive the government can be to the changing will of the people under socialism. Though we have not examined the question fully as yet, we have seen that, from the economic point of view, a socialistic economy must be a planned economy, and economic plans cannot be made and carried out on a day to day basis. The very notion of economic planning seems to imply that national economic plans, once they are made, should be followed persistently through at least a reasonable period of time. The government could not be expected, for example, to spend a couple of years developing additional productive facilities for the production of shoes and then abandon this equipment and start building facilities for automobile production because the tastes of the citizens in consumption had changed in the meantime. At best, it would seem that the government could respond to the changing will of the people in regard to economic matters only at reasonable intervals, and this whole discussion in any case slides over the difficult question of how the government would ascertain the popular will on a hundred and one matters with any great accuracy.

As the above discussion suggests, the government under socialism would probably be responsible to the popular will only in the sense that, if the planners do not give the people what they want in a given period of, say, four or five years, the citizens will rise up at the next election, throw the rascals out of office, and substitute a set of planners who will make plans which are better suited to the desires of the people. But this may be easier said than done, for there is a grave question as to whether full-fledged economic planning is compatible with the democratic process. Economic planning requires that enormous powers be concentrated in the hands of certain governmental agencies which are charged with the making and enforcement of economic plans, and these great powers might be used to destroy democratic control of the government. The planners may come to think that they know what the people need and desire better than the people themselves know and, if this happens, one of the principal plans which the planners work on may be a scheme for keeping themselves in office. Thus, some people think that economic planning under socialism is more likely to be associated with dictatorship than with democracy.

In theory, it would be possible to guard against this danger. The planning agencies could be made creatures of the legislature, the legislature could specify the general goals toward which economic planning should be directed, it could reserve the right to ratify all plans before they would go into effect, and it would have the right to recall members of planning agencies who functioned unsatisfactorily. Although such technical safeguards would be desirable, the real answer to the question of whether national economic planning is compatible with democracy depends probably on the question of what human nature would be like under socialism. It would depend on the idealism, altruism, and motivation in general of the leaders of the government and economic system. Many people will believe that a country can have both economic planning and democracy only when they see it, and certainly little can be found in the operation of the Soviet Russian economy to date to suggest that economic planning on a national scale is likely to be associated with democracy in government.

Finally, there are several problems in connection with economic representation. It is easy to say that representation in the legislature should be economic in character, but which industries and occupations should be represented, and which should be excluded or lumped together? How many legislators should there be on this basis, how should they be apportioned among industries and occupations, and how should minorities in industries or occupations be represented? Even more important, would economic representatives function more efficiently than representatives of states or of given numbers of people? Would they know more about the important economic questions on which they would have to decide and would they be better able to take a broad social point of view in their deliberations? These questions could be answered definitely only on the basis of experience. Many people would contend that our national legislators already actually represent major economic interests rather than states or numbers of individuals. If this is true, the government of socialism would merely bring economic representation out in the open. In any case, we might expect to find combinations and blocs of legislators, pressure groups, log-rolling, and other features of our capitalistic government under socialism. However, the socialists contend that these things would lose much of their significance under socialism, since opportunities for private profit would be eliminated almost completely. For example, some legislators

might try to convince the rest that the economy should develop increased electric power by means of generating plants which burn coal, while others might stand for the development of hydroelectric power, but, with both types of electric plants owned and operated by governmental agencies, no groups of private citizens would be able to make private profits whatever the decision of the legislature might be.

### *The Government of Soviet Russia*

*The Revolution and Early Government* We must now leave our speculations as to what government might be like in socialistic systems which do not yet exist and turn to an examination of the government under which the socialistic system of Soviet Russia actually operates. In this discussion, we must concentrate our attention very largely on the Russian government as it exists at present and deal only sparingly with earlier governmental systems. Before 1917, the government of Russia had been a constitutional monarchy in name. In fact, however, despite the various concessions which the tsarist government had made as a result of the unrest and discontent of the people, the government was still a practically absolute monarchy, and an extremely corrupt and bureaucratic one at that. After several years of rather unsuccessful participation in World War I on the side of the Allies, the corruption and inefficiency of the tsarist government became unbearable, and this government came to its end by revolution early in 1917. In March of that year, there were spontaneous uprisings of great masses of people in the leading cities and the Tsar, Nicholas II, was compelled to abdicate his throne, since he had lost the support of the armed forces of the nation. Groups of workers, known as "soviets" or councils, sprang into action in the chief industrial centers, attempted to preserve order, and administered the food supplies. A provisional government, under the authority of the lower house of the legislature, was established and operated for a time under the leadership of Kerensky.

This provisional government, however, followed a dilly-dallying policy and in several months' time made little progress toward setting up a genuinely stable government. As a result, in the fall of 1917, the Bolshevik Party took over the reins of government. This party was a rather small left-wing or revolutionary group, but it had

control of some local soviets, especially those in Moscow and Petrograd, and believed it could command the support of the masses On November 6, 1917, the government buildings and facilities in Petrograd were taken over and the Kerensky government fell An All-Russian Congress of Soviets, welding together the various local soviets of workers, was called in session and it undertook the formation of a new government, under the guidance of the Bolshevik Party (later to become the Communist Party of the Soviet Union) Legislative and executive authority was vested in a so called Council of People's Commissars, with Lenin at the head

In its first few years, the new government was kept extremely busy in resisting attempts at counter-revolution at home and in fighting off the troops which Russia's former allies sent into the country, so the details of governmental organization developed slowly The federal constitution which completed the organization of the Union of Soviet Socialist Republics (USSR) was not adopted until 1923 Lenin died in 1924, and Trotsky and Stalin began their famous struggle to see who would be the new leader of the party and the government Stalin, of course, was the ultimate winner and has been the real head of government and party to this day

*The Government of the USSR, 1923-1936* The government of the Union of Soviet Socialist Republics, under the 1923 Constitution, was organized as a federation of four republics, but the number of republics eventually became seven through some internal redistribution of territory Though the government was federal in form, power was strongly centralized in the national government, which had jurisdiction over all external affairs of the country, and all internal matters which were of national importance The leading agency of government was nominally the All-Union Congress of Soviets, or national legislature This body, since it contained over 2000 representatives, was most unwieldy and could never really function as a legislature It actually met only once in three or four years, instead of once in two years as scheduled, and its sessions were most perfunctory That is, the members would merely listen to tales of the exploits and plans of the leaders of the Communist Party and elect the so-called All-Union Central Executive Committee, which wielded the legislative powers in the periods between sessions of the legislature The Presidium, or presiding committee of the legislature, was also of considerable importance

The federal government was not divided into departments, as is

that of the United States, for the highest executive agency of the government, the Council of People's Commissars, was elected or appointed by the legislature, or one of its subsidiary bodies, and the judges of the courts and state prosecutors were also appointed by and responsible to the legislature. The State Planning Commission, which had charge of making the economic plans for the country as a whole and supervising their operation, was a committee appointed by the Council of People's Commissars. The various republics which made up the system had governmental organizations quite similar to that of the U S S R as a whole. The various agencies and organizations of government were actually of comparatively little importance, for the real governmental power of the system resided in the Communist Party and its leaders.

On the surface, it appeared that the right to vote was to be enjoyed by practically all persons, for the Constitution extended this right to all citizens, 18 years of age or over, who performed productive, socially useful labor, to members of the army and navy, and to citizens who would ordinarily be workers but who were incapacitated for some reason or other. In practice, the franchise was by no means universal because of the way in which productive, socially useful labor was defined. Among those who were disfranchised were employers of labor, private traders and business men, receivers of unearned income, monks and members of the clergy, members of the royalty, police, and secret service under the old tsarist regime, lunatics, and persons who had been convicted of disgraceful crimes. Elections were indirect in character. The actual voters of the country elected only the members of local soviets. The members of the local soviets elected the members of regional soviets, and so on up to the All-Union Congress of Soviets, which was actually several times removed from the elections in which the voters had participated.

Elections were by open ballot, that is, by voice vote or show of hands, rather than by secret ballot as in the United States. Some citizens voted from ordinary electoral districts, while others voted from factories or other economic units. Representation in the national legislature was disproportionate for different groups of voters. Industrial workers, for example, were allowed one representative for every 25,000 voters, while peasants could have only one representative for every 125,000 voters. Thus, the majority of the members of the legislature were representatives of industrial workers and something like three-fourths of the representatives were also mem-

bers of the Communist Party Finally, under the old government, the rights of the individual were extremely limited Freedom of speech, freedom of the press, freedom of assembly, and other common rights of the individual, were unknown Even justice was administered on a "class" basis If an individual became involved in court action, the first question addressed to him was likely to concern his social origin, and the same set of facts might produce quite different court decisions according to whether the individual had a satisfactory social origin as an honest, upright worker or an unsatisfactory one as a former member of the nobility or as an employer (and presumably exploiter) of labor

*The 1936 Constitution* The governmental organization of Soviet Russia was changed to a considerable extent by the adoption of a new federal Constitution in December, 1936 This document declares the U S S R to be a socialist state of workers and peasants, with basic political power residing in the working people through their soviets In such a socialistic economy, there is to be social ownership of the tools and means of production, though social ownership may be taken to mean in general either state or cooperative ownership Land, natural resources, waters, forests, and some other things are definitely state property Small-scale personal enterprises are tolerated if they involve no exploitation of labor Individuals are permitted private property in their income from work, personal savings, dwelling houses, auxiliary husbandry, household articles and utensils, and articles for personal use and comfort Such personal property may be inherited The economy is to operate on the basis of economic planning in order to increase the public wealth, improve the material and cultural standards of the people, and strengthen the country's independence and capacity for defense All citizens who are able to work must do so if they expect to eat The general principle of income distribution is that each person is to produce according to his ability and to receive income according to the work which he accomplishes

The Constitution provided for a federal union which included eleven constituent republics at the beginning Later the number of republics was increased to sixteen, both by redistribution of territories within the country and by the acquisition of new territories Lithuania, Estonia, and Latvia were "admitted" to the U S S R as constituent republics on August 3, 5, and 6, 1940, while in the same year Bessarabia was taken into the Moldavian autonomous republic,

making the latter a constituent republic, and the Karelian-Finnish republic was created. Though the government is federal in form, most governmental powers are in the hands of the central government and the republican governments have only such powers as are assigned to them. Among the matters controlled by the federal government are foreign relations, the admission of new republics, enforcement of the Constitution, supervision of the Constitutions of the republics, to see that they are consistent with the federal Constitution, boundary changes and internal redistributions of territory, national defense and domestic security, organization of the judiciary and preparation of civil and criminal codes, legislation concerning the right of citizenship and the position of foreigners, the right of amnesty, the foreign trade monopoly, the federal budget and taxation, the administration of banking, industrial, agricultural, and commercial enterprises of All-Union importance, transportation and communication, money, credit, insurance, and state loans, and the determination of fundamental principles in connection with land use, exploitation of natural resources, education, health, accounting, and labor legislation.

The individual republics are guaranteed cultural autonomy and the right to use their own languages. They also have the nominal right to secede from the union, but actually any attempt to exercise this right would probably be regarded and dealt with as treason. The various republics are supposed to be equal partners in the union, but one of them, the Russian Soviet Federative Socialist Republic, actually outweighs all the others put together. As the eleven original republics were constituted in 1922, the R S F S R had about nine tenths of the total area of the country, two thirds of its population, and its two largest cities, Moscow and Leningrad. The governments of the republics are quite similar to the federal government in organization.

*The Supreme Soviet of the U S S R.* The highest agency of the present government of Soviet Russia is the Supreme Soviet of the U S S R., or national legislature. It is made up of two houses, whose members serve four-year terms. The members of one house, known as the Soviet of the Union, are chosen from electoral districts on the basis of one member for each 300,000 of population. The other house, called the Soviet of Nationalities, contains twenty-five representatives from each constituent republic, eleven from each autonomous republic, five from each autonomous region, and one

from each national region In 1941 there were 647 representatives in the Soviet of the Union and 713 in the Soviet of Nationalities<sup>4</sup> The membership of each house is not fixed, since the number of representatives in the Soviet of the Union will vary with changes in population whereas the number in the Soviet of Nationalities will be altered as the number of republics and other subsidiary governmental units changes with the redistribution of old territories and the admission of new territories to the union The Supreme Soviet is supposed to meet twice a year and each house elects one president and two vice-presidents The houses have equal rights in all legislative matters, and bills pass by a simple majority in each house Besides its legislative powers, the Supreme Soviet has the power to amend the Constitution by a vote of two-thirds of its members

The Presidium of the Supreme Soviet is a sort of executive committee of the legislature and has most of the powers of the legislature when the latter is not in session It is a body composed of 42 members and is elected by the Supreme Soviet It convenes and dissolves the Supreme Soviet, calls new elections, holds referendums, interprets the laws of the land and issues administrative decrees, revokes orders and decisions of the Council of Ministers if they do not conform to the law, removes and appoints members of the Council of Ministers, grants decorations and honors, exercises the right of pardon, appoints and dismisses the high command of the armed forces, declares war, orders mobilization, ratifies and denounces treaties, and appoints and recalls ambassadors The Presidium continues to function in the interval between the end of one legislature and the election of the next It is required to call new elections within two months after the dissolution of the old legislature and to call the new legislature together within one month after an election Thus, we see that the Presidium has a considerable number of legislative and administrative functions, especially when the legislature is not in session To be sure, many of its acts require the later approval of the Supreme Soviet, but this approval is quite sure to be given since both the Supreme Soviet and the Presidium are ultimately controlled by the Communist Party

<sup>4</sup> E. J. Simmons, editor, *USSR A Concise Handbook*. Ithaca, New York Cornell University Press, 1947, p. 160

*The Council of Ministers* The U S S R , under its present government, continues to have a cabinet type of executive That is, the highest executive and administrative agency of the government is the Council of Ministers (known until 1946 as the Council of People's Commissars), the members of which are elected by the Supreme Soviet This agency, which is, of course, subsidiary to the Supreme Soviet and responsible to it, has a Chairman and ten Vice-Chairmen and includes all the Ministers and the Chairmen of the Committee on Arts, the Committee on Higher Education, the Administration of the State Bank, and the State Planning Commission The Council of Ministers functions by issuing decrees based on existing laws It coordinates the work of the various governmental departments or Ministries, and has important functions to perform in connection with the making and administration of economic plans (through the State Planning Commission), the administration of money and credit, and the execution of the state budget It also adopts measures pertaining to the maintenance of public order, the protection of the interests of the state and of the citizens, and the organization of the armed forces of the nation, and creates commissions or other agencies to deal with military, economic, and cultural matters

*All-Union Ministries* The individual Ministers, who make up the greater part of the Council of Ministers, have charge of the work of their particular departments in much the same fashion as do the cabinet officers of other countries These departments, or Ministries, have an important place in the Soviet Russian scheme of things, for, in many cases, they are both governmental departments and departments controlling specific phases of the economic life of the country As such, they form one of the main connecting links between government and the economic activities of the system The Ministries are divided into two general classes, the All-Union Ministries and the Union-Republic Ministries The All-Union Ministries, as their name implies, deal with matters which are of great importance to the country as a whole or which seem to require uniform administration all over the country The affairs of these Ministries are administered through branches or agencies in lower governmental units of the country, and the individual republics as a rule do not have departments of their own to deal with the same matters Since the Ministries of both types are in an almost constant process of reorganization, there seems to be no point in trying to give a com-

plete list of either type of Ministries However, the All-Union Ministries include, among others, those of Armaments, Automobile Industry, Aviation Industry, Chemical Industry, Coal Industry, Communications, Electrical Industry, Ferrous Metallurgy, Foreign Trade, Heavy Machine Building, Higher Education, Machine Tools, Merchant Marine, Non-ferrous Metallurgy, Petroleum Industry, Railroads, River Transport, and Shipbuilding<sup>5</sup>

*Union-Republic Ministries* The Union-Republic Ministries deal with matters which, though not unimportant to the whole country, show considerable variation from one area to another and seem to require somewhat different treatment in the various republics Such matters are placed in the joint jurisdiction of federal and republic governments, and the Union-Republic Ministries operate through similar ministries in the individual republics The Union-Republic Ministries include those of Agriculture, Armed Forces, Control, Finance, Fishing, Food Industry, Foreign Affairs, Internal Affairs, Justice, Light Industry, Livestock, Public Health, State Security, Textile Industry, Timber Industry, Internal Trade, and others<sup>6</sup>

*Other Administrative Agencies* The State Planning Commission (Gosplan) is a sort of sub-committee of the Council of Ministers In many ways, it is the most important single economic agency in the country, for it has direct charge of making the national economic plans and supervising their fulfillment Its work will be discussed in detail in Chapter 6 For several years, another agency known as the Commission of Soviet Control was also attached to the Council of Ministers Its duty was to assure the actual execution of governmental orders and decrees with promptness and efficiency and to weed out graft, bureaucracy, and incompetence Its membership was closely controlled by the Communist Party, and it was able, through the assistance of a large staff of agents, to bring offenders directly to justice However, this Commission was replaced by the newly created Ministry of Control in 1940, and this new Ministry now oversees and controls the expenditure of governmental financial and material resources, and verifies the execution of official decisions

In 1940, six Economic Councils were created and attached to the Council of Ministers They are for Metallurgy and Chemistry, Machine Building, Defense Industry, Fuel and Electric Power, Con-

<sup>5</sup> *The Soviet Union Today* New York The American Russian Institute, 1946,  
p. 26  
<sup>6</sup> *Ibid.*, p. 26

sumers' Goods, and Agriculture and Procurements, and are intended to coordinate the work of the various Ministries which fall in their respective fields Two other agencies, known as the Council of the State Bank and the Committee for State Defense, are also attached to the Council of Ministers The Committee for State Defense was set up as a kind of war cabinet in 1941, at the time of the Nazi invasion and consisted of Stalin, V M Molotov, K E Voroshilov, L P Beriya, and G M Malenkov.

*The Judiciary* Under the present Russian government, the judiciary, like the executive, is subsidiary to the legislature The Supreme Soviet appoints the Attorney General of the USSR for a term of seven years He in turn appoints States Attorneys for the republics, regions, and provinces, and approves the appointment of District Attorneys for lower governmental units The judges of the lowest courts, called People's Courts, are elected for three-year terms by the voters of local areas by direct secret ballot These courts handle both civil and criminal cases, but not, in general, very important cases The territories, provinces, and regions have also courts whose judges are elected by the Soviets, or legislatures, of these various governmental units These courts deal with more serious criminal cases, such as those involving counter-revolutionary activities or theft of socialist property, and with civil cases involving governmental units or public institutions The republics have supreme courts whose judges are elected by the legislatures for five-year terms Finally, at the top of the heap there is the Supreme Court of the USSR, with judges elected by the Supreme Council for five-year terms The membership of this court includes 45 judges and 20 assessors

The Constitution provides for the equality of all citizens before the law, for uniformity of civil and criminal procedure throughout the country, for the independence of judges, for the use of local languages in the courts, for the right of persons accused of crimes to legal defense (in most cases), for publicity with regard to court proceedings (in most cases), and for an elective judiciary In many of the courts, cases are handled by a judge and two assessors, or by a group of three judges in some cases The so called assessors are representatives of the citizens and receive only the wages of their regular employments while serving in the courts All citizens are apparently qualified to function as judges or assessors, since there seem to be no educational or other requirements for these positions

*The Rights of Citizens* The individual citizens of the U S S R are highly privileged individuals, if we may rely upon the various guarantees which the 1936 Constitution affords The citizens are guaranteed freedom of speech, freedom of the press, and freedom of assembly, processions, and demonstrations, but with the proviso that these rights must be used in the interests of the working people and for the strengthening of the socialist state Cultural, scientific, and technical organizations, youth organizations, trade unions, co operative associations, and (for especially worthy citizens) the Communist Party are among the organizations permitted to exist The Constitution grants freedom from arbitrary arrests, the inviolability of homes, secrecy of personal correspondence, the equality of all citizens, freedom of conscience, the separation of church and state, freedom of religious worship and of anti-religious propaganda, the right to work, the right to leisure, the right to education, and the right to material security The franchise is now extended to all citizens aged 18 or over who are not insane and have not been deprived of the right to vote as the result of being convicted of crimes Elections are direct and by secret ballot Candidates for office are nominated in the appropriate electoral districts by units of the Communist Party, social organizations of workers, trade unions, cooperative societies, youth organizations, and cultural societies

*Nature of the Communist Party* It is difficult to obtain an understanding of the actual operation of the government of the U S S R by studying merely the various governmental organizations and the functions which are allotted to them by the Constitution Regardless of such organizations and functions, political and governmental power in Soviet Russia is completely concentrated in the hands of the Communist Party In other words, the Communist Party completely dominates the government of Soviet Russia and has its members in practically all important offices and positions Its will is done by all governmental agencies and organizations We now turn to a brief study of this all-powerful Party

The Communist Party operates on the basis of a charter adopted in 1934 and amended in 1939 According to this prospectus, the Party is

the organized vanguard of the Proletariat in the U S S R , the highest form of class organization The Party leads the proletariat, the toiling peasantry, and all toiling masses in the struggle for the dictatorship of

the proletariat, for the victory of socialism. The Party is the leader of all the organs of the proletarian dictatorship and assures the successful building up of the socialist society. The Party is a united fighting organization bound up by conscious iron proletarian discipline. The Party is strong through its unity, its singleness of will and a singleness of action incompatible with deviation from the program, with breach of party discipline, or with the formation of factions inside the Party.<sup>7</sup>

*Communist Party Membership.* Applicants for membership in the Communist Party must be at least 18 years of age and must agree to live up to certain requirements, which include unity of doctrine and practice, implicit and complete obedience to Party authority, and the famous "vow of poverty" by which the applicant agrees to be content with a salary not substantially greater than that of a skilled and zealous manual worker.<sup>8</sup> All applicants, except former members of other political parties, must be endorsed by three Party members of at least three years' standing who have known the applicants as fellow workmen for at least one year. These applicants may be admitted to full membership after spending one year as "candidates" or "probationary members." Former members of other political parties require the consent of the Central Executive Committee of the Communist Party in order to become members and must spend three years as candidates.

In theory, full members of the Party have numerous rights, including the right to hold office and vote in Party elections, the right to criticize any member at the various Party meetings, the right to request information from or make representations to any Party official or organization, and the right to present testimony when their personal conduct is under investigation. These rights imply the existence of democracy within the Party and the determination of Party policies by a process of lively discussion and debate. Actually, however, Party policies are strictly laid down by a small number of Party leaders and little discussion is permitted. Moreover, the qualifications of Party members are frequently reexamined from the point of view of individual character and behavior, ideological orthodoxy, and general devotion to the cause of the Party, and those members who are found wanting are cast into the outer darkness. One estimate has it that in the period from 1934 to 1939 some 466,000 members (almost 25 per cent of the total) and 516,000

<sup>7</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, pp. 96-97.

<sup>8</sup> Sidney and Beatrice Webb, *Soviet Communism A New Civilization?* New York: Charles Scribner's Sons, 1936, pp. 347-350.

candidates (or over 50 per cent of the total) were purged from the Party.<sup>9</sup> Apparently these purges eliminated many of the older members of the Party, for, after they were over, about half of the members of the Party Congress were 35 years of age or less and another third of the members were under 40.<sup>10</sup> Thus, over 80 per cent of the members of the Party Congress were so young that it is scarcely possible that they could have been members of the Bolshevik Party before the Revolution or have taken part in the Revolution.

Membership in the Communist Party is ordinarily a greatly desired privilege in Soviet Russia, for it brings the individual prestige and possibly power, as well as certain economic advantages with respect to travel, rations and shopping rights (at times), and the securing of desirable living quarters. Nevertheless, membership in the Party has been held down to a remarkably low level. In 1941, for example, the Party included only 2,515,481 members and 1,361,404 candidates for membership.<sup>11</sup> During World War II, there was a rapid expansion in membership to 5,000,000 or 5,800,000,<sup>12</sup> but even such a membership constitutes a very small minority, or something less than 3 per cent of the population. Data on the internal structure of the Party are difficult to obtain, but roughly three-fifths of the members are supposed to be industrial workers, and farm workers or peasants may make up about one-fifth of the membership.

From time to time, the Party has refused to admit new adult members, and, in any case, it intends to depend largely on its various youth organizations for its new members. In this way, it secures young and enthusiastic members who have been brought up along Party lines and have been thoroughly educated in Party principles. The youth organizations include the All-Union Leninist Communist League of Youth (Comsomols) which has some 15 million members, aged from 14 to 23, of whom half were acquired during World War II, the Children's Communist Organization of Young Pioneers in the name of Comrade Lenin (Young Pioneers) whose members are from 10 to 16 years of age, and the little Octobrists who are from 8 to 11 years of age.

*Communist Party Organization* The organization of the Com-

<sup>9</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, p. 111.

<sup>10</sup> *Ibid.*, p. 111.

<sup>11</sup> *The Soviet Union Today*, p. 30.

<sup>12</sup> *Ibid.*, and E. J. Simmons, editor, *USSR A Concise Handbook*, p. 156.

unist Party is rather complex. At the bottom there are many thousands of local Party units or cells. These may exist in any factory, store, collective farm, state farm, army unit, or other organization which contains at least three Party members. These local cells are supposed to play an active part in the political and economic life of Soviet Russia. Under the supervision of higher Party organizations, they attempt to improve the discipline of the workers and spur them on toward the fulfillment of planned goals, attend to the political education and training of prospective members, and propagandize and agitate for the fulfillment of the system's economic plans. Above the local cells, there are Party organizations for towns and cities, territories, and republics. In general, each unit is responsible to the next higher unit in the hierarchy, and its officers must be approved by the next higher unit. The nominal head of all Party organizations is the All-Union Congress of the Communist Party, which included 1567 voting delegates when it met in 1939.<sup>13</sup> The Congress is supposed to convene at least once in three years, but it is obviously too large to be the effective head of the Party and its meetings were suspended altogether after 1939.

When the Congress did meet, it voted unanimously to approve the accomplishments, plans, and proposals of the Party leaders and elected a Central Executive Committee, of 71 members and 68 alternates, to function in its stead. This Committee, in turn, appoints several other agencies which seem to control the actual operation of the Party. One of these, the Political Bureau or Politburo, originally consisted of only five members (Lenin, Stalin, Trotsky, Kamenev, and Bukharin) but has now been increased to ten. It has complete control over the policy-making powers of the Party and hence of the government. The other agencies are the Organization Bureau (Orgburo), which deals with questions of personnel, and the Central Control Commission, which keeps Party members in line and purges the unreliable.<sup>14</sup>

*Democracy or Dictatorship?* What sort of a government is produced in the end by this combination of democratic constitution and strong single political party? On the basis of the democratic constitution and the fact that the leader of the Communist Party, Joseph Stalin, had not (until recent times) held any important gov-

<sup>13</sup> *Ibid.*, p. 157

<sup>14</sup> *Communism in Action*. Washington: 79th Congress, 2nd Session, House Document No. 754, pp. 97-98.

ernmental office, some writers conclude rather optimistically that the government of Soviet Russia is a democracy in fact as well as in theory Thus, the Webbs hold that the Communist Party is merely a "vocation of leadership" and that its position in the Russian scheme of things is something like that which a Roman Catholic order, such as the Society of Jesus, has or formerly had in a Roman Catholic country They claim that the Party influences or controls the policies and actions of individuals or governmental agencies only by persuasion and that, if the Party wields actual political and governmental power, it does so by "keeping the conscience" of its members and getting them elected to office by a genuinely popular vote<sup>15</sup>

On the whole, however, there is little difference of opinion as to the actual nature of the present government of Soviet Russia In spite of the democratic facade which the constitution provides, the government is a dictatorship of the most absolute and complete variety, with the leaders of the Communist Party in full control In the first place, the Party dominates the electoral process In theory, any citizen can run for office and be elected In actual elections, while several candidates (for the legislature, say) may be nominated in each electoral district, all of the candidates except one usually withdraw before the election is held and only one candidate in each district is actually presented to the voters The surviving candidates are those fortunate individuals who have the approval of the Party, although they are not necessarily all Party members Moreover, they are likely to run for office on the basis of a platform sponsored by the "election bloc of Party and non-Party people," which would make any independent candidate almost automatically a counter-revolutionary In the 1937 elections, 96.8 per cent of the eligible voters went to the polls and 98.6 per cent of the votes cast favored the single candidates sponsored by the Party<sup>16</sup> Moreover, 81 per cent of the members elected to the Soviet of the Union and 71 per cent of those elected to the Soviet of Nationalities, were members or probationary members of the Communist Party<sup>17</sup> After 1937 there were no new elections to the Supreme Soviet until February, 1946, when 110,000,000 voters, or almost all those eligible, went to the polls and again showed startling unanimity in voting

<sup>15</sup> Sidney and Beatrice Webb, *Soviet Communism A New Civilization?* p 310

<sup>16</sup> M T Florinsky, *Toward an Understanding of the U.S.S.R.*, p 112

<sup>17</sup> *Ibid.*, p 142

for the official candidates Such results, of course, would be unthinkable under a real democracy

Again, the Communist Party maintains Party offices or agencies to match the various offices and agencies of the government The soviets or councils of localities, districts, regions, provinces, and republics are paralleled by Party units or organizations in all these geographical subdivisions The All-Union Congress of the Communist Party is the counterpart of the Supreme Soviet, or national legislature, the Central Executive Committee of the Party is similar to the government's Council of Ministers, and so on through the long list of governmental offices and agencies In practically all cases, there is a considerable duplication of personnel between the Party and governmental offices and organizations At the end of World War II, Stalin was Secretary-General of the Party, member of the Orgburo and Politburo, chairman of the Council of Ministers, and Supreme Commander-in-Chief Six vice-chairmen of the Council of Ministers were also members of the Politburo Zhdanov, the chairman of the Supreme Soviet, was a member of the Secretariat, Politburo, and Orgburo of the Party, and so was Malenkov, one of the members of the Presidium<sup>18</sup>

The results of these conditions are not at all difficult to imagine The Supreme Soviet is a mere figurehead Its members approve the accomplishments and proposals of the Party leaders unanimously and almost without discussion, laws desired by the leaders are passed automatically, and the persons appointed by the Supreme Soviet to be judges, prosecutors, or members of the Council of Ministers are those who are approved and suggested by the Party leaders The Party itself apparently has considerable legislative powers, for its leadership issues directives with the force of law to various government departments and many laws come into force under the joint signature of the Party Secretary and the Chairman of the Council of Ministers The various governmental officers pursue objectives which are laid down by the Party leaders and use methods approved by these same authorities, while the State Planning Commission makes its economic plans for the country as a whole on the basis of general goals or objectives which are provided by the Party leaders In all governmental and economic matters, there is no overt opposition to the will of the Party as expressed by its leaders

<sup>18</sup> *Communism in Action*, p. 98

As if these things were not enough, the Party has at its disposal an elaborate organization for the "protection of the regime." It maintains a large and well-trained secret police, which has had virtually unlimited powers, including that of life or death over the individual, and which operates largely outside the courts and established judicial procedure of the country. This secret police (N K V D) is intended to discover and destroy all counter-revolutionary and anti-state activities. Counter-revolutionary activities are said to include any actions directed toward the overthrow, undermining, or weakening of the government of the U S S R or parts of the basic economic, political, or national conquests of the proletarian revolution, the undermining of State industry, transportation, commerce, money and credit, or cooperative activities, or the intentional nonfulfillment of definite duties or negligence in their fulfillment with the intent of weakening the Soviet Power or disorganizing state machinery. Anti-state activities include actions which are not counter-revolutionary but which lead to the disorganization of the regular functioning of the administrative or economic organs of government and involve resistance to such organs, interference with their work, violations of laws, or other activities which weaken the power and integrity of the State. Clearly, this organization has the power to crush completely any latent opposition to the Communist Party. Under its widespread and efficient operation, the various rights which the Constitution "guarantees" to the individual citizen (with respect to freedom of speech, freedom of the press, freedom of assembly, freedom from arbitrary arrest, the inviolability of homes and correspondence, and other matters) mean very little if anything.

In particular, the guarantee of freedom of religion is thought to have been honored in the breach by the Communist government of Russia, but this is not altogether surprising in view of the alleged unsavory character of the former Russian Orthodox Church. The last Tsar, as absolute head of the Church, had the disreputable monk, Rasputin, as his spiritual adviser. The village priests were uneducated and venal, the monasteries have been called "nests of miracle-mongering," and the church in general mixed a great deal of superstition and pagan magic with its religious services and rites. After the revolution, many excesses were committed against the Church. The properties of churches and monasteries were confiscated, priests were disfranchised, deported, placed in confinement,

or even killed, and churches were transformed into clubs, granaries, and warehouses.

In later years, before World War II, the attitude of the government toward religion moderated somewhat. In fact, there was freedom of religion in a restricted sense. There was apparently no law against the belief in or practice of religion; religious services were held, events such as births, marriages, and deaths could be solemnized by religious rites, and religious training could be given by parents in the home. On the other hand, this freedom of religion was counteracted by freedom of anti-religious propaganda, and the government was definitely on the anti-religious side of the question. The church was completely separated from the state and from the educational processes of the country; it was a serious offense to propagandize in favor of religion; no religious books could be published or imported, and church groups could not operate foundations, charities, or recreational projects. The government operated anti-religious museums and in general was persistent in its efforts to convince the people that religious activities were rather simple and stupid and that they have no place in the modern socialized economy.

During World War II the Russian government and Communist Party came to take a much more favorable attitude toward religion. The church cooperated actively with the government in the prosecution of the war, and it came to be defined as a useful and loyal element in society. Soviet citizens were allowed to attend religious services freely, additional churches were opened, anti-religious propaganda came to an end, godless publications were suspended, and anti-religious museums were closed. In 1943, Stalin declared that the government would have no objection to the election of a Patriarch of the Russian Orthodox Church, denied since 1925, and one was duly elected. The government permitted the publication of a monthly magazine by the Patriarchate, and a holy-candle factory was started. Permits were issued for the opening of ten theological seminaries by August 1, 1945. Religious instruction was no longer restricted to the home but could be given to groups of children in the churches. The church was permitted to print materials for use in its services and could order quantities of testaments, prayer books, and liturgical books.<sup>10</sup> These changes depended upon government permissions, rather than on new legislation, and

<sup>10</sup> *Ibid.*, pp. 129, 131.

it remains to be seen whether they represent a new permanent policy or only a temporary expedient deemed appropriate under wartime conditions

The Communist dictatorship also helps to perpetuate itself through its absolute control over the educational system of Russia. According to official reports, Soviet Russia is making enormous strides in increasing the numbers of students in schools and colleges and in reducing illiteracy, but there is no doubt that the educational process is used for political purposes. That is, the teachers must be "politically reliable" and the task of the students is, above all else, to learn devotion to socialism, economic planning, and the principles of the Communist Party. Opportunities for discussion, as contrasted with learning by rote, are extremely limited, especially in connection with social and economic matters.

Finally, the Communist dictatorship strictly controls the leisure-time activities of the citizens.

The amount of time allotted a worker depends upon the type of work he is engaged in and the quality of his performance. The places to which he may go in search of rest and recreation are likewise determined for him. The groups within which his leisure time activities are performed are organized and activated by Communist Party members. The sports in which he participates are designed to strengthen his physical power and skills for military and for labor purposes. His cultural activities during leisure time are further conditioned by the political control of newspapers and books, plays or movies, and radio programs or musical concerts.<sup>20</sup>

If there is any thought that our description of the Russian dictatorship is overdrawn, we may say that some writers deal much more harshly with the subject. One writer, for example, has suggested that the Russian system is really capitalistic in character, with the Party leaders occupying the places of the former capitalists. The ordinary citizens receive a bare subsistence, and all income above this minimum goes to the Party leaders and bureaucracy. The "vow of poverty" and Party maximum salary are said to have been mere myths for many years. Party members receive salaries which run up to 30 times as high as those of ordinary workers, and high Party officials enjoy eight-room apartments, numerous servants, the use of country estates and rest homes, fleets of automobiles with chauffeurs, and plentiful quantities of all kinds of scarce consumers' goods. Most of the work is done by various specialists, such as

<sup>20</sup> *Ibid.*, p. 125

engineers, scientists, accountants, and technicians, who receive both moderate salaries and blame for everything that goes wrong Thus, while the lives of Party officials may be short, they should be merry<sup>21</sup>

The N K V D. is accused sometimes of conducting a reign of terror and of punishing many rather innocuous activities as counter-revolutionary Among the things which have led to severe punishment as counter-revolutionary actions, wrecking, or sabotage are refusing to set impossible goals for economic plans, slowing down production to avoid the breakdown or rapid deterioration of machinery, refusing to falsify accounts and records to please the leaders, trying to get a fair price for exports and so selling less than planned amounts, complaining about such things as hours, wages, or food rations, or failing to "volunteer" to work overtime or on "free" days when asked by Party officials The victims of the N K V D are said to be seized without warrant, condemned without trial, and sent to prison camps where, in the face of inhuman tasks with the death penalty for non-fulfillment, most of the prisoners die and the others eke out a horrible existence With many industries operated by convict labor, the N K V D is said to play an important part in the economic functioning of the system<sup>22</sup>

It is difficult to discover the exact extent to which these additional charges against the Communist Party and its dictatorship are true, but there is no doubt about the existence of the dictatorship itself, with control in the hands of the leaders of the Communist Party The control of the Party extends not merely to economic and political affairs but to such matters as education, religion, and other social institutions as well The Russian dictatorship is the very antithesis of that political and economic democracy which modern socialists expect to have in their ideal system

#### QUESTIONS

- 1 "The government in a capitalistic economy must be democratic, while those of socialistic, communistic, and fascist economies are necessarily dictatorships" Discuss

<sup>21</sup> Freda Utley, *The Dream We Lost* New York The John Day Company, 1940, pp 222 225

<sup>22</sup> *Ibid*, pp 227 230 and 238 239 *Communism in Action*, pp 54 58 D J Dallin, *The Real Soviet Russia* New Haven Yale University Press, 1944, pp 237 244

- 2 Must the government of a capitalistic economy follow a policy of *laissez-faire* with regard to economic activity?
- 3 "In practice, the governments of capitalistic economies interfere with economic activity to a considerable extent and own and operate numerous enterprises and industries" Illustrate
- 4 Precisely what do socialists mean when they say that the government of their ideal system would be a democracy? Explain
- 5 Indicate the problems which might be encountered in attaining the type of government which the socialists propose
- 6 "The government of a socialistic system might be set up as a democracy, but it would develop into a dictatorship before very long" Show whether you agree
- 7 Compare the actual government of Soviet Russia with the government proposed by modern socialists for their ideal system
- 8 How does the federal government of Soviet Russia differ from the federal government of the United States? Explain
- 9 In what important respects does the present government of Soviet Russia differ from that which prevailed between 1923 and 1936?
- 10 "In the United States, the powers of the federal government are divided among three branches, known as the executive, the judiciary, and the legislative departments. Each of these departments has carefully circumscribed functions and is rather independent of the other departments" Compare this situation with that which exists in Soviet Russia
- 11 Discuss the significance of the Communist Party in connection with the government of Soviet Russia
- 12 How does the Communist Party control the government of Soviet Russia?
- 13 "Russia at the present time has a highly democratic constitution but her government is an absolute dictatorship" Show whether you agree
- 14 "In answer to the question of whether Soviet Russia is a political democracy, it is clear that, on the basis of the 1936 Constitution, the U S S R. is the most inclusive and equalized democracy in the world" Show whether you agree
- 15 "If the Russian government actually lived up to the 1936 Constitution, it would closely approximate the government proposed by modern socialists" Do you agree? Explain

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## CHAPTER 4

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### GOVERNMENT

(Continued)

#### *The Government of Britain under Partial Socialism*

**The Constitution** The government of the United Kingdom of Great Britain and Northern Ireland has been regarded by many people as almost a model of democratic government. It operates under what is usually called an unwritten constitution, but this means merely that the constitution, unlike that of the United States, is not contained in any single document and has to be pieced together from a large number of enactments, such as the Magna Carta, the Bill of Rights, the Habeas Corpus Act, and the Parliament Act. In addition the constitution includes a number of conventions which are generally regarded as binding even though they are not a part of any formal statute. The constitution of Britain can be amended at any time by an ordinary Act of Parliament. Thus Parliament extended its own life in 1939, in order to avoid an election during wartime, in spite of the rule which requires an election of Parliament at least once in every five years.

**The King** Although the King is the nominal head of the British government, he really has only one important constitutional function—that of choosing a new Prime Minister when the incumbent dies or resigns. He must approve all laws enacted by Parliament, but has no veto power. He is the head of the Church of England and, on the advice of the Prime Minister, appoints Bishops and Archbishops. He is also nominal head of the Army, Navy, and Air Force, and of the executive department of government—all state property being vested in him. In practice, the King is most important as a kind of elder statesman in the government and as a living symbol of Great Britain and the British Empire.

*The Legislature* The supreme agency of government in Britain is the legislature, or Parliament. Any law passed by both houses of Parliament not only must be accepted by the King but is also absolutely binding on the courts. The House of Commons has 517 members from England, 74 from Scotland, 36 from Wales, and 13 from Northern Ireland, or a total of 640. The qualifications for membership in the House of Commons are very mild. With only a few exceptions, any British citizen who is 21 years of age may be elected, and there is no residence requirement. It is rather common for a constituency to elect someone who lives in an altogether different section of the country. Elections must normally be held at least once every five years but they are usually held whenever the Government is defeated on a vote of confidence in the house, and also whenever the Prime Minister decides that an appropriate time has arrived for testing the opinion of the country. Special elections, called by-elections, are held whenever a member of the House dies or resigns.

The House of Lords has about 750 members, including the Royal Dukes, the hereditary peers of Great Britain (of whom there are about 675), 16 representative peers of Scotland, 14 representative peers of Ireland, 7 Lords of Appeal in Ordinary, and 26 Lords Spiritual (the Archbishops of Canterbury and York and 24 Bishops). Most of the work of the House of Lords is done by members who have received their titles during their lifetime instead of inheriting them. While the House of Lords actually passes legislation as well as debates matters of general importance, its legislative powers are strictly limited. Any "money bill," or one which contains only provisions concerning taxation or the payment or appropriation of public funds, becomes law even if the Lords do not pass it, provided that it is sent up to the Lords at least a month before the current session ends. Moreover, any bill passed by the House of Commons on three occasions over a period of at least two years will become law even though the House of Lords does not approve it.

It is clear, then, that the House of Commons is the more important part of the legislature, but this does not necessarily mean, as Gilbert and Sullivan said in *Iolanthe*, that the House of Lords "does nothing in particular but does it very well." Some bills are actually originated in the House of Lords, and others which come up from Commons are amended both in form and in substance. Moreover, through its powers to delay the passage of most

types of bills for two years, the House of Lords may perform a useful function in preventing the enactment of hasty or extreme legislation by the House of Commons.

*The Prime Minister and Cabinet* The executive department of the British government is headed in practice by the Prime Minister and his Cabinet. When a new Parliament has been elected, it is the King's duty to select the Prime Minister from the political party which has a clear majority in the House of Commons. This task is not usually difficult, for each party normally has a leader who is all groomed for taking over the position of Prime Minister, but the situation may become complicated if no one party has a clear majority in the House. The Prime Minister in turn chooses his Government, including members of the Cabinet and other less important Ministers. The number of Cabinet members is variable, but usually runs between 20 and 25. Certain positions in the Government, such as the Lord Chancellor, the Chancellor of the Exchequer, the Home Secretary, and the First Lord of the Admiralty, always entitle the holders to be members of the Cabinet, but others may or may not.

While they remain in power, the Prime Minister and Cabinet have almost complete control over the whole machinery of government. In other words, the legislature, while supreme in power, will do as the Prime Minister and Cabinet ask, as long as it has confidence in them, and, if it loses confidence, the Government will be overthrown and a new Prime Minister and Cabinet selected. In particular, all responsibility for raising and spending money is concentrated directly in the Prime Minister and his Cabinet. The primary function of the Cabinet is to initiate and sponsor legislation. In the recent war period all legislation was official and individual members could not introduce bills, but even in peacetime about 90 per cent of all laws enacted by Parliament are introduced by members of the Government. Most Cabinet members are also heads of governmental departments and are responsible for their administration. While most of the detailed executive work is done by permanent officials (Permanent, Second, Principal Assistant, and Assistant Secretaries, and their underlings), it is the Ministers who are responsible to Parliament. Thus, the Cabinet has charge of the general policy and administration of the government. It usually functions as a body because, except under most unusual circumstances, the entire Cabinet falls if one of its members falls.

*The Judiciary and Court System* The court system for criminal cases in Britain runs all the way from the local courts conducted by magistrates, or justices of the peace, up through Petty Sessions, Quarter Sessions, and Assize Courts to the Court of Criminal Appeal. Police officers take charge of the prosecution in numerous less important cases, but in others solicitors or barristers may represent the prosecution. There is also a Director of Public Prosecutions who handles the prosecution in murder cases and others which cannot be handled in the usual way. The court system for civil cases runs from the County Courts at the lowest level up to the Court of Appeal, the High Court of Justice, and the House of Lords, which hears a limited number of cases on appeal each year. The judges of most of the courts are appointed by the Lord Chancellor, though some are selected by the Prime Minister. As previously noted, no courts have the power to declare laws unconstitutional.

*Individual Rights* The citizens of Britain for many years have enjoyed virtually the complete list of individual or civil rights. With the exception of peers, criminals, and lunatics, every man and woman over the age of twenty-one has the right to vote. It is a fundamental principle of British law that individuals cannot be detained in custody except on a specific criminal charge or conviction, and the courts are required to look into every detention of an individual if they are called upon to do so. British citizens have freedom of the press, subject only to the laws of sedition and criminal libel, and freedom of speech provided that they do not infringe the laws against sedition, blasphemy, disorderly conduct, and so on. Freedom of assembly is also virtually complete. In spite of the fact that there is an established church in England, the English citizens, like those of other parts of Britain, have complete freedom of conscience in matters pertaining to religion. These rights of British citizens do not depend in general on specific guarantees embodied in the constitution, as in the United States. They depend rather on the continued vigilance of the public and the common sense of twelve men in the jury box in individual cases, which make everyone connected with British government reluctant to take any action which might interfere with individual freedom.

*British Government under Socialism* The government of Britain which we have described so briefly is not only democratic in character but also seems to correspond fairly well to the model set up by modern socialists for their ideal system, as described in the

preceding chapter Since the Labor Party secured control of the government, and the right to put its program of partial socialism into effect, through the customary process of winning a general election (in July, 1945), many people conclude that in Britain we shall have our first valid example of a country which combines socialism in economic matters with democracy in government.

However, Winston Churchill, the leader of "His Majesty's loyal opposition in the House of Commons," charged, in October, 1947, that the socialist rulers of Britain were stripping the people of their hard-won liberties and reducing them to helpless servitude.<sup>1</sup> His indictment contended that the Labor Government is making every effort to keep people from going abroad, that it is exercising censorship over newspapers in effect by manipulating the paper shortage and other shortages, that the government is opening individuals' letters on the pretext that people may be sending valuables out of the country (a policy which might readily develop into the persecution of individuals whose ideas are unfavorable to the present regime), and that the government has asserted its power in time of peace to choose or change the occupations of the individual citizens. Mr Churchill complained further that the Labor Government has made the daily lives of the people subject to literally thousands of regulations and controls in the enforcement of which a multitude of government officials, larger than any army which Britain had maintained in peacetime in the past, is continually employed. Finally, he said, the government has invented hundreds of new crimes for which imprisonment or penal servitude may be inflicted. While these charges were probably not without some political bias, the fact that they could be made in late 1947, before the program of socialism in Britain had more than gotten well under way, suggests that we might well wait a while before concluding that socialism in Britain will be able to combine large-scale economic and social planning with a full measure of individual rights and liberties, and democracy in government.

### *The Government under Fascism*

In the present discussion of fascist government and in later chapters we shall use Germany and Italy as examples of the fascist type of system. Many of the other countries which are sometimes

<sup>1</sup> *The Chicago Tribune*, October 5, 1947

placed in the fascist category either did not have nearly so clear cut a development of fascism as did Germany and Italy or were far less important economically.

*The Rise of Fascism in Italy* The Fascist movement in Italy arose out of the confusion and chaos which prevailed after World War I. Dissatisfaction with the results of Italian participation in the war was general. The cost of the war in terms of wealth and manpower had been heavy, inflation had placed severe burdens on the Italian citizens, and depressed economic conditions after the war had thrown large numbers of industrial employees out of work. Moreover, Italian gains from the war seemed trifling and insignificant. Italy faced serious problems of economic readjustment and seemed unable to get started toward their solution.

The Italian government apparently could not take decisive action in the postwar emergency. Political parties were numerous in the Italian system and it was generally impossible for any one party to obtain clear-cut control of the government. The result was a succession of short-lived coalition governments which were incapable of dealing effectively with the problems of the day. Since the political leaders who had carried Italy into and through the war were both exhausted and discredited in the eyes of the people, the government lacked leadership and there seemed to be no one who could form and maintain a really stable government. At times it even appeared that the Italian system might be overthrown by a socialist or communist revolution. During the war period, the membership of the Italian Confederation of Labor had increased by about ten times, and many of the trade union members were also affiliated with socialist, communist, and syndicalist organizations. Strikes, riots, general strikes, sit-down strikes, and other disturbances marked the early postwar period and caused great concern.

The Fascist movement had its beginning in March, 1919, when Benito Mussolini, formerly a revolutionary socialist, and a rather small band of followers founded the first of the *Fasci di Combattimento*, or fighting squads, at Milan. This original organization was soon duplicated in many cities and towns all over Italy. For some time after their organization, the new Fasci lived up to their name of "fighting squads," for their chief activity seemed to be fighting with opposing groups, and especially with the Socialists and other

radical organizations, and their participation in political activity was conspicuously unsuccessful.

The question of what the Fascists stood for in these early days is not an easy one to answer. Their party program for the 1919 elections was liberal and democratic, if not downright socialistic in character. However, it became clear that they could not catch many political fish with this bait and, as strikes, riots, and conflicts with the Socialists and other radical groups increased in number and severity, they turned rather quickly to a strongly nationalistic and anti-socialistic policy. In this way, the Fascists were able to attract the support of large numbers of industrialists, landowners, professional men, shopkeepers, students, and former soldiers and army officers. The workers, for the most part, belonged to the various radical groups. In its early days at least, Fascism was anything but a working-class movement.

With increasing support all over the country, the Fascists became even more aggressive politically and moved toward power by means of methodical violence. The tactics of the Fascists bore some fruit in the 1921 elections, for thirty-five Fascists, ten Nationalists, and several sympathizers were elected to the Chamber of Deputies, with Mussolini as the leader of the group. In 1922, conditions in Italy went from bad to worse. Riots and civil disturbances increased in number and intensity, the rapidly changing cabinets of the government became more and more powerless to deal with the emergency and achieve law and order, and the Fascist Party increased in numbers and strength until in October it was ready to make an attempt to take over the government of Italy. It was on October 26, 1922 that some fifty to seventy thousand Fascists began the famous "March on Rome," led by the Fascist *quadrumvate* of Balbo, Bianchi, De Vecchi, and De Bono, while Mussolini waited in Milan. Faced with this situation, the cabinet made a desperate attempt to act at the last moment and declared a state of martial law, but the King refused to sign the decree. Instead, he summoned Mussolini to the capital and appointed him Prime Minister.

The Fascist government did not immediately become a dictatorship. In the beginning, the Fascists had control over only about 50 members out of 535 in the Chamber of Deputies, or lower house of the national legislature, and the first cabinet was of the coalition variety, since it contained several non-Fascist ministers. However, the Chamber of Deputies, by a vote of 215 to 80, gave full power

to the new government for a year so that it might pursue certain necessary reforms without the limiting influence of parliamentary formalities. The Fascist government proceeded to steal much of the thunder of opposition groups by reducing taxation, balancing the budget, and enthusiastically pushing a program of social legislation and low-cost housing. Some of the activities of the government were very unpopular with large numbers of Fascist Party members and a split within the Party ensued. The Party was then "reorganized and purified," tens of thousands of members were ousted, and control of the Party was even more strongly centralized in the hands of Mussolini.

Any hopes that the Fascist Party, now that it was in power, would settle down to sobriety and moderation in its political activities were quickly dashed. Mussolini had increased the regular army from 175,000 to 275,000 men, and the former fighting squads of the Party were reorganized into a Blackshirt militia of 190,000 men, sworn to the personal service of *Il Duce*. The program of violence and suppression of the opposition continued apace. In the summer of 1923, the Party forced a new electoral law through the legislature, which provided that the party which secured the largest number of votes in an election would be entitled to two-thirds of the seats in the Chamber of Deputies, with the other seats being divided among the remaining parties in proportion to the votes received. The following election of April, 1924, solidified Fascist control over the Chamber of Deputies. Finally, in January, 1925, Mussolini announced that further cooperation with opposition groups had become impossible and that henceforth the Fascist Party would rule the country on the basis of a one-party system, without the assistance of the gentlemen of the opposition.

From this point on, the opposition was simply overwhelmed. Many repressive laws were passed, labor organizations were eliminated, political parties and cultural societies were smashed, the newspapers were bought off, muzzled, or destroyed, all personal rights and liberties of individuals were taken away, governmental positions were filled with loyal Fascists, and the old organizations of government completely lost their power. The genuine dictatorship of the Fascist Party had begun and the government was remolded along the lines of the new Fascist political philosophy.

*The Rise of Fascism in Germany* The condition of Germany in the first few years after World War I was even worse, if possible,

than that of Italy In spite of tremendous hardships and sacrifices, Germany had "lost" the war, the emperor had abdicated, and the government had been overthrown The Treaty of Versailles, which Germany had signed under considerable duress, held her responsible for the war, compelled her to make reparations payments, limit armaments, and demilitarize the Rhineland, and imposed serious direct losses of resources and facilities for production Before Germany could get well started along the road to economic recovery, she was prostrated again by the terrible period of currency inflation which culminated in 1923 The value of the mark depreciated tremendously and prices rose to astronomical levels Investors, people with fixed incomes, and members of the middle class in general were extremely hard hit and, in most cases, completely ruined by the inflation, while unscrupulous speculators were able in some cases to amass large fortunes In the latter days of the inflationary period, production, employment, and economic activity in general were at low ebb

It was in these troubled years after the war that National Socialism (fascism) got its start Adolph Hitler, soon to be the leader of the movement, was unknown in 1919 He was an Austrian, had migrated to Germany in 1912, had served in the war as a corporal in the army, and had been wounded and gassed In 1919, he attended a meeting of the so-called German Workers Party, a political organization of only 28 members, which had been founded in the same year by one Anton Drexler, a locksmith Hitler joined the party, becoming its leader in 1921, and its name was changed to the National Socialist German Workers Party The Party adopted an official program or platform written by an engineer named Gottfried Feder The platform contained a great deal of nationalism and some ideas which might be construed as socialistic, but very little indeed to indicate that the Party represented the interests of the workers It also contained a strong flavor of racialism or anti-Semitism, which the name of the Party did not seem to imply On the whole, the platform clearly indicated a desire to appeal to a large number of classes of people and to be all things to all men

In spite of its many-sided appeals for support, the National Socialist Party did not grow nearly so rapidly as its leaders had hoped it would Nevertheless, Herr Hitler, in collaboration with General Ludendorff, led the organization into a revolt against the Republican government of Bavaria in November, 1923 If this

venture had succeeded, the Nazis might have come into power in Germany only about a year after the Fascists had seized control in Italy. However, the revolt failed, and Hitler was arrested, tried, and convicted, along with many of his henchmen. Because of the moderation of the government then in power, Hitler received merely a short prison term for his treasonable activities. During his stay in prison, he is supposed to have written his book, *Mein Kampf*, which was to become the Party Bible. At this time, the National Socialist movement was at low ebb.

In the years from 1924 to 1929, Germany was at peace and enjoyed a fair degree of prosperity, though her economic recovery seems to have resulted largely from huge loans secured abroad for purposes of reconstruction and improvement. While the prosperous period seems to have been of the "Indian Summer" variety, the National Socialist Party made relatively little progress during the period. In the elections of May, 1928, for example, the Party received only some 800,000 votes and captured only 12 seats in the Reichstag. However, the period of the great depression was distinctly another story. The depression arrived early in Germany, and its economy suffered greatly because of its incomplete recovery from the war. International trade almost disappeared, the sources of foreign credit dried up, and the number of the unemployed grew to 6,000,000 or about a third of the number previously employed. It soon appeared that the system could not continue as it was. That is, either the conservative groups, such as industrialists and landowners, would have to take strong action to retain their dominant position, or some radical group or groups would come into power and alter the system to their liking.

The German labor organizations had grown steadily in numbers and power since 1924, and many of their members belonged also to the various radical political parties. Strikes, picketing, and mass demonstrations were very disturbing to the conservative groups. It is a much disputed question whether the radical groups could actually have taken over the governmental and economic system, since these groups were so numerous and so completely unable to get along and cooperate with each other, but there is little doubt that the German industrialists and landowners were desperately afraid that Communism was in prospect. In this situation, these conservative groups apparently turned to the National Socialist Party as a possible bulwark against Communism. The Party had

something of a following among the lower middle-class group, whose support was needed by the industrialists and landowners, and the Party itself seemed about as confused as the people it was trying to attract. The Party program contained some elements calculated to please almost all groups in the population, and it seemed (at the time) that it could be made into almost anything and used for almost any purpose. At any rate, leaders of the conservative groups conferred with Hitler, and the Party received financial and other support from the industrialists and landowners, both openly and secretly.

The power of the National Socialist Party grew rapidly in the depression period. The votes which it was able to command increased from 800,000 in 1928 to 6,409,000 in September, 1930, and 13,779,000 in July, 1932. However, the total vote obtained by the Party fell off to 11,737,000 in November, 1932.<sup>2</sup> In 1932, Hitler was defeated for the presidency by von Hindenburg, but even in defeat he received 11,300,000 votes on the first ballot and 13,400,000 in the run off election.<sup>3</sup> In November, 1932, Hitler was offered a position in the cabinet of the national government, but he refused to serve. Finally, in January, 1933, after another cabinet crisis, he was called in by President von Hindenburg and made Chancellor of the German Reich. National Socialism had come into power.

Many factors played a part in the rapid growth of the National Socialist Party after 1928, in addition to the important measure of support given by the landowners and industrialists. One was undoubtedly unemployment. Large numbers of recruits to the Party came from the ranks of the unemployed, including as many as 60 to 70 per cent of those joining the Storm Troopers in the large cities.<sup>4</sup> Again, the children of the war years had just come of age. Many of them had experienced only unemployment, hardship, and poverty, had lost all faith in the existing system, and were ready to follow any leader who promised a way out. As one writer has said, members were attracted to the Party by its militant character, the thrills and novelty, the uniforms, the fights, and the heroic trappings and phraseology. It offered a strange mixture of brutality, racial pride, anti-Semitism, vague radicalism, romanticism, and sen-

<sup>2</sup> K. Leowenstein, *Hitler's Germany*. New York: The Macmillan Company, 1939, p. 3.

<sup>3</sup> M. T. Florinsky, *Fascism and National Socialism*. New York: The Macmillan Company, 1936, pp. 42, 43.

<sup>4</sup> *Ibid.*, p. 43.

timentality which just seemed to suit the confused young citizens of Germany.<sup>5</sup> Other factors often mentioned were the magnetic personality and effective oratory of the leader of the Party, the skillfully staged mass meetings, the improved Party organization, the constant campaign of propaganda and agitation, and the clever lies and distortions of the truth which the Party placed before the people.<sup>6</sup>

The Party also grew because of its ability to appeal to several different classes of people. The early members of the Party have been referred to as "Maladjusted demobilized professional soldiers, soldiers of fortune, social misfits, and cranks, white collar proletariat of frustrated intellectuals and unemployed clerks—a strange motley of hooligans, criminals, and idealists."<sup>7</sup> Later, in 1928 and after, members were recruited from the lower middle class and finally from the industrialists and landowners. The army was rather indifferent to the development of the movement, while Socialists, Communists, Catholics, and, in general, the laboring masses were not tempted by the glittering prospectus which the party offered.

Under the Weimar Republic, the German government which was replaced by the system of National Socialism, Germany had had a parliamentary form of government modeled after the French and English systems. The chancellor and the ministers were responsible to the Reichstag, which was elected by universal suffrage and proportional representation. The second chamber of the legislature, the Reichsrat, was made up of representatives of the various German states. The president was elected by popular vote for a seven year term and could succeed himself indefinitely. The system also provided for direct legislation by way of popular initiative and referendum.

However, in spite of various concessions which were obtained from Germany's former enemies in regard to the application of the provisions of the peace treaty, the government under the Weimar Republic was never able to get rid of the stigma which was attached to it because it had (very unwillingly) yielded originally to the demands of the Allies. Moreover, the democratic government provided by the Weimar Republic functioned none too well in the hands of a German people who were accustomed to autocracy and

<sup>5</sup> *Ibid.*, pp. 43-45.

<sup>6</sup> K. Leowenstein, *Hitler's Germany*, pp. 5-7.

<sup>7</sup> *Ibid.*, pp. 4, 5.

government by force In the fourteen years from 1919 to 1933, 20 cabinets under 12 chancellors came into power and soon departed, while no less than 38 separate political parties took part in the 1932 Reichstag elections The Weimar Republic, though liberal in its treatment of labor, left much political and economic power in the hands of large industrialists and landowners, and it had a succession of important crises to handle, with only a few years in which economic life could be regarded as even close to normal Finally, the government suffered by being exceedingly considerate of its enemies, who were left relatively free to agitate against the government, plan and execute treasonable acts, and in general develop to the point at which they could take over the government If Hitler's rebellion in 1923 had been staged against a government like that of Soviet Russia, he would undoubtedly have been transported quickly and efficiently from this life, and the world might have been spared an unmeasurable toll of grief and suffering

The first cabinet under National Socialism contained only three National Socialists (Hitler, Frick, and Goering) among its eleven members However, Hitler was Chancellor, Frick was Minister of the Interior, and Goering was Minister without portfolio, Commissioner of Air Communication, and Commissioner of the Interior for Prussia Thus all the police organizations of the country were under the control of these Nazi ministers, and the Party was free to subdue and liquidate the opposition groups The new government quickly dissolved the Reichstag and called a new election for March 5, 1933 In spite of intensive preparation by the Party for a "controlled election," prospects of victory were apparently not developing as well as the leaders thought they should be, and the famous Reichstag fire was staged on February 27, a little over a week before the election While a weak-witted Dutch Communist named van der Lubbe was indicted, tried, and executed as a scapegoat in connection with the fire, there is little doubt that the conflagration was executed by the National Socialists themselves, as an excuse for dealing harshly with the various radical groups and for using all kinds of violence and intimidation in the election period

On February 28, the day after the fire, President von Hindenburg suspended the constitutional provisions relating to freedom of speech, freedom of the press, freedom of assembly, and other civil rights In this way, the police acquired virtually unlimited powers for dealing with all "offenders against public order and security"

The election came off as scheduled, with the Iron Front, composed of Socialists, Communists, and the radical and democratic parties in general, competing against the National Front, which included the National Socialist Party and the German National Party. The National Socialists received 17,300,000 votes and 288 seats in the Reichstag, while the German National Party secured 3,100,000 votes and 52 seats. This gave the National Socialists and their allies a clear majority of the 608 seats in the Reichstag, a majority which was increased by barring a considerable number of radical members from their seats. From this point on, the dictatorship of National Socialism made rapid progress.

### *The Fascist Philosophy*

***The Individual and the State*** Probably the most basic idea in the fascist philosophy of government was that of the supremacy or superiority of the state in relation to the individual.

The key-stone of the Fascist doctrine is its conception of the State, of its essence, its functions, its aims. For Fascism the State is absolute, individuals and groups relative. Individuals and groups are admissible in so far as they come within the State. Instead of directing the game and guiding the material and moral progress of the community, the liberal State restricts its activities to recording results. The Fascist State is wide awake and has a will of its own. For this reason it can be described as "ethical."

The State, as conceived and realised by Fascism, is a spiritual and ethical entity for securing the political, juridical, and economic organisation of the nation, an organisation which in its origin and growth is a manifestation of the spirit. The State guarantees the internal and external safety of the country, but it also safeguards and transmits the spirit of the people, elaborated down the ages in its language, its customs, its faith. The State is not only the present, it is also the past and above all the future. Transcending the individual's brief spell of life, the State stands for the immanent conscience of the nation. The forms in which it finds expression change, but the need for it remains.<sup>8</sup>

Thus, in the fascist philosophy, the nation was much more than the sum total of the individuals who composed it at any particular time. The nation had a life, and ends or objectives, of its own. These goals could be perceived only dimly, if at all, by the individual citizens, and might well be opposed, in many cases, to the

<sup>8</sup> B. Mussolini, *Fascism Doctrine and Institutions*. Rome: Ardita Publishers, 1935, pp. 27-28.

ends which individuals would seek if left to their own devices In all such cases, the ends of the state or nation should be pursued, rather than those of private individuals, because of the superior importance of the national objectives Individuals were important, not for their own sake, but merely as the means by which the nation might reach its objectives They were considered as temporary and insignificant particles in the long life of the state

The subordination of the individual to the state was not for his own good, but for the good of the state and for the attainment of its objectives Since the state is, for all practical purposes, a mythical concept, this means that the individual was subordinated to the party leaders who controlled the government, in order that the objectives which these leaders deemed appropriate for the nation might be achieved The individual was conceived of only as a part of the nation As the fascists said, apart from the collective group the individual had no more purpose or reason for being than has a body cell apart from the human body as a whole The single body cell had no rights on which it could insist in opposition to the human body as a whole, and it would be equally ridiculous to think of the individual citizen as having any rights which were superior to those of the state and which the state must respect Thus, the individual had no rights, but merely duties to the state which he was expected to fulfill at any cost As compensation for his lowly individual status, the citizen was supposed to find satisfaction and glory in the achievement of national goals

*Fascism and Democracy* With this general attitude toward the relationship of the individual to the state, it followed naturally that the fascists had nothing but contempt for democracy Ordinary individuals were thought to be too ignorant or too completely immersed in the private affairs of life to be allowed to participate actively in government and control governmental policies

Fascism trains its guns on the whole block of democratic ideologies, and rejects both their premises and their practical applications and implements Fascism denies that numbers, as such, can be the determining factor in human society, it denies the right of numbers to govern by means of periodical consultations, it asserts the irremediable and fertile and beneficent inequality of men who cannot be levelled by any such mechanical and intrinsic device as universal suffrage Democratic regimes may be described as those under which the people are, from time to time, deluded into the belief that they exercise sovereignty, while all the time real sovereignty resides in and is exercised by other and sometimes irre-

sponsible and secret forces Democracy is a kingless regime infested by many kings who are sometimes more exclusive, tyrannical, and destructive than one, even if he be a tyrant<sup>9</sup>

Since the processes of democracy were repudiated, the power to rule under fascism was to be located in the hands of those relatively few individuals who, as a result of the "irremediable and fertile and beneficent inequality of men," were politically elite—able, courageous, and strong-willed Needless to say, these individuals in Italy and Germany, according to the fascist notion, were found exclusively in the fascist party Within the elite group, there must be discipline, order, hierarchy, and unquestioning obedience to the leader Strangely enough, however, the fascists asserted that the government produced thus was not really a dictatorship but rather that it allowed the individual citizens the maximum of liberty.

A state based on millions of individuals who recognise its authority, feel its action, and are ready to serve its ends is not the tyrannical state of a medieval lordling It has nothing in common with the despotic States existing prior to or subsequent to 1789 Far from crushing the individual, the Fascist State multiplies his energies, just as in a regiment a soldier is not diminished but multiplied by the number of his fellow soldiers The Fascist State organises the nation, but it leaves the individual adequate elbow room It has curtailed useless or harmful liberties while preserving those which are essential In such matters the individual cannot be the judge, but the State only<sup>10</sup>

**Fascism and Socialism** The fascists declared themselves to be opposed unalterably to socialistic doctrines of peace and internationalism Fascism was aggressive and warlike, as well as strongly nationalistic

First of all, as regards the future development of mankind—and quite apart from all present political considerations—Fascism does not, generally speaking, believe in the possibility or utility of perpetual peace It therefore discards pacifism as a cloak for cowardly supine renunciation in contra-distinction to self-sacrifice War alone keys up all human energies to their maximum tension and sets the seal of nobility on those peoples who have the courage to face it All other tests are substitutes which never place a man face to face with himself before the alternative of life or death Therefore all doctrines which postulate peace at all costs are incompatible with Fascism Equally foreign to the spirit of Fascism, even if accepted as useful in meeting special political situations, are all internationalistic or League super-structures which, as history shows,

<sup>9</sup> *Ibid.*, pp. 21-22

<sup>10</sup> *Ibid.*, pp. 29-30

crumble to the ground whenever the heart of nations is deeply stirred by sentimental, idealistic, or practical considerations.<sup>11</sup>

Fascism also rejected the emphasis which socialists place on the importance of economic affairs in the life of men and in determining the course of history.

Such a conception of life [as the Fascists have] makes Fascism the resolute negation of the doctrine underlying so called scientific and Marxian socialism, the doctrine of historic materialism which would explain the history of mankind in terms of the class struggle and by changes in the processes and instruments of production, to the exclusion of all else. That the vicissitudes of economic life—discoveries of raw materials, new technical processes, scientific inventions—have their importance, no one denies, but that they suffice to explain human history to the exclusion of other factors is absurd. Fascism believes now and always in sanctity and heroism, that is to say in acts in which no economic motive—remote or immediate—is at work. Having denied historic materialism, which sees in men mere puppets on the surface of history, appearing and disappearing on the crest of the waves while in the depths the real directing forces move and work, Fascism also denies the immutable and irreversible character of the class struggle which is the natural outcome of this economic conception of history, above all it denies that the class struggle is the preponderating agent in social transformations. Having thus struck a blow at socialism in the two main points of its doctrine, all that remains of it is the sentimental aspiration—old as humanity itself—toward social relations in which the sufferings and sorrows of the humbler folk will be alleviated. But here again Fascism rejects the economic interpretation of felicity as something to be secured socially, almost automatically, at a given stage of economic evolution when all will be assured a maximum of material comfort. Fascism denies the materialistic conception of happiness as a possibility, and abandons it to the economists of the mid-eighteenth century. This means that Fascism denies the equation well-being = happiness, which sees in men mere animals, content when they can feed and fatten thus reducing them to a vegetative existence pure and simple.<sup>12</sup>

*The Economic Philosophy of Fascism.* In this attack on socialism, we see once more the fascist attitude toward economic matters in general. Apparently the fascists believed that capitalist economies are best methods to pursue undesirable, or at least relatively unimportant, objectives. Private property, free enterprise and competition are useful institutions and even economic moderation is, within limits, not undesirable. The methods and practices of capitalist exploitation are also acceptable. But all these things should

<sup>11</sup> p. 15, 16  
<sup>12</sup> p. 1, 21

not be directed toward the mere maximization of production or the improvement of the standard of living of the individual citizens. These things are not appropriate goals for a nation. The political or other aims of the state are the supreme ends, and all economic programs, policies, and results are merely means toward their accomplishment. Since the economic institutions of capitalism, if left alone, might operate to produce the results desired by private individuals rather than those which are desirable for the nation, the state must intervene and control their operation in its own interests. If the achievement of the aims of the state results in low standards of living for the individual citizens, this latter result is relatively unimportant. Thus, in spite of the nominal nature of the economic institutions of fascism, it is clear that the fascist state aimed to rule in the economic sphere as completely as in others. We shall see later what all this meant in terms of specific economic policies and practices.

*Racialism* The fascist philosophy was the same in most essential respects in both Germany and Italy, but in Germany it contained one element which was not duplicated in Italy for several years. This was its strong racialism and anti-Semitism. The hatred of the Jews and the desire to reserve all good things in Germany for true Germans was present in the German fascist movement from the very beginning. According to the official doctrine, true Germans were of the Nordic or Aryan race. The Jews were by contrast an inferior and treacherous race which had to be eliminated from the population before Germany could become truly great. This racialism became embodied in many official acts of government, and many unofficial (but nevertheless governmentally inspired) acts of violence and destruction, as we shall see later.

### *Fascist Government*

The Italian government under Fascism continued to operate on the basis of the same fundamental law as formerly, known as the Statute of 1848. Since the Fascist "revolution" did not actually eliminate the old form of government and set up a new one in its place, it was really more of a *coup d'état* than a revolution. Though the basic law remained the same as before, the actual government of Italy was changed in many respects under Fascism. These changes were possible in part because the Statute of 1848 was written in

vague and general terms which would permit a great deal of stretching and broad interpretation. It was also true that the Italian system of government contained no supreme court which had power to interpret the basic law and declare laws or acts of the government invalid in the light of the basic law. Thus, while the ultimate sovereignty rested in the hands of the citizens or people under the Statute of 1848, it was possible for the Fascists to transfer the sovereignty in fact to the state, which meant to the leaders of the government.

The government of Germany under National Socialism actually operated without any constitution, although the Weimar Constitution was never formally amended or repealed. The government in effect had the power to change the Constitution at will, and the Constitution and the courts were completely unable to restrict the activities of the government. The famous "Enabling Act" of March 24, 1933, gave the executive arm of the government the power to make laws by decree and specified that such laws could deviate from the Constitution if they did not affect the Reichstag or Reichsrat or the powers of the President. Even these limitations on the decree laws were removed as of January 30, 1934. 8178

*The Executive Department* Italy under Fascism remained a kingdom with a hereditary King as nominal head of the state, but the King was a pure figurehead after he performed his fatal function of appointing Mussolini to be Prime Minister in 1922. In Germany, after the death of President von Hindenburg in August, 1934, Hitler took over the Presidency by decree and added it to his offices as Chancellor and Party Leader. Despite such differences, governmental powers were concentrated most completely in the hands of the great dictators, Hitler and Mussolini. They appointed and dismissed cabinet ministers and other officials, summoned and dissolved the legislatures, commanded the armed forces, controlled the introduction and passage of all laws or made laws by decree, ruled the court systems, dominated lower units of government, and were supreme in the field of foreign relations.

Hitler and Mussolini, as Chancellor and Prime Minister, were heads of cabinets, whose members included the Ministers in charge of the customary array of government departments. The dictators appointed, directed, and removed cabinet members at their discretion. The Ministers were subordinates and trusted henchmen, but not colleagues, and were personally responsible to the dictator.

Each Minister had considerable power in his own department, but cabinet meetings were held rather infrequently and differences between the Ministers were resolved directly by the dictator rather than by debate. In Germany, the make-up of the cabinet changed very little through time. In the first seven years of the regime, a total of only nineteen men served as heads of the various ministries, and nine ministers (out of fifteen) remained unchanged through this period.<sup>13</sup> In Italy, there was a more rapid turnover in the cabinet positions, and Mussolini often held several cabinet posts besides serving as Prime Minister.

**The Legislature** With governmental powers concentrated in the executive department and in particular in the hands of the dictator, the legislature declined rapidly in importance in the fascist countries. In Italy, the upper house of the legislature, called the Senate, was not changed to any great extent under fascism. It consisted of about 500 life members appointed by the King, upon recommendation of the Prime Minister. Except for sitting as a high court of justice in certain types of cases, it had no very important duties to perform, and it was commonly described as a conservative forum of elderly high nobility and propertied gentry, or as a club composed of noted persons, since it contained educators, literary figures, diplomats, and scientists, as well as church officials and members of the nobility and royal families.

The lower house of the Italian legislature was altered significantly under fascism. As the Chamber of Deputies it was elected in the usual fashion until 1928, when a law was passed which provided for a new method of selecting the members of the Chamber. When an election was in the offing, the syndicates of employers and employees, and certain other groups, were entitled to select a list of 1000 candidates from which the Grand Council of the Fascist Party would choose 400 names to be placed, as a national list, before the voters, who could vote "yes" or "no" only for the list as a whole. Only Fascists of proved loyalty were nominated; speeches in opposition to the official candidates were not permitted, the Grand Council (or cabinet) of the Fascist Party could remove any deputy, and the "yes" and "no" ballots were of different colors so that anyone could see how an elector voted. Thus the "representatives" in the Chamber of Deputies did not really represent the people at all, except in the most general sort of way. The members of the Chamber were hand-

<sup>13</sup> K. Leowenstein, *Hitler's Germany*, pp. 34-36.

picked Fascists who would obey the will of the dictator without deliberation and without question.

Even this distorted vestige of the democratic electoral process eventually became distasteful to Mussolini, and the Chamber of Deputies was replaced in 1938 by a new body called the Chamber of Fasces and Corporations. This group included the head of the government, 25 members of the Fascist Grand Council, 120 members of the National Council of the Fascist Party, and 500 members of the National Corporative Council, or almost 650 members in all. The new Chamber was a hasty perennial since its members required no election and remained in office indefinitely. It was also completely under the thumb of the dictator, since all its members were selected by Mussolini.

The legislative power in Germany, as in Italy, was exercised by the executive branch of the government and especially by the dictator himself. As we have noted, the Enabling Act of 1933 gave the executive almost unlimited powers for a period of four years and the right to make laws by decree. This law was renewed periodically in later years. The Reichsrat, or upper house of the legislature, was abolished in February, 1934, but the Reichstag continued to exist. Under the Nazis its membership increased to more than 800 deputies, all selected by Party leaders from the membership of the National Socialist Party.

In both countries, the function of the legislature was supposedly collaboration with the government in the formation of laws. This meant, in effect, that it initiated no legislation, considered only the business which was suggested to it by the executive, and approved enthusiastically any proposals of the executive. The Reichstag, for example, met briefly only 11 times in the first six years of National Socialism and passed only five laws. In reality, the legislatures were probably kept to give the fascist regimes the appearance of legality, to rubber-stamp governmental policies which had been previously determined by the executive, and to serve as cheering sections and sounding boards for Party propaganda and the speeches of the dictators.

*The Court Systems.* Both fascist countries retained in general the court systems which had existed previously, though courts, judges, and officials at all levels of government were brought under the direct control of the national Ministries of Justice. Moreover, the court systems were "purified" through the removal of politically

unreliable (and, in Germany, Jewish) judges and officials Law ceased to exist as an objective concept That is, the law of the land depended from day to day on the changing will of the dictators, and the judges had become loyal party men who were ready and willing to follow the leaders' whims

The fascists added several types of courts to the old systems and in particular set up special courts for the defense of the state and the regime against various treasonable activities and political crimes. Both countries also set up and maintained secret police forces (the Gestapo in Germany, for example) which operated at least in part beyond and outside the formal government and were charged with ferreting out individuals engaging in treasonable activities and political crimes, or who might be thinking of doing so, and bringing them to "justice" The methods of the secret police included the inspection of private correspondence, the tapping of telephone lines, the use of dictaphones, spies, and informers, the control of passports and border traffic, military and economic espionage and counter-espionage, the expatriation of enemies living abroad, and a thorough and constant check-up on party members

Many harrowing tales were told of the fate of persons brought before these special courts by the secret police Trials were held at once and in secrecy, accused persons either were not permitted the services of lawyers or were assigned, at great expense, lawyers who were greatly hampered in their efforts to defend their clients, no witnesses for the defense were permitted, and the judges who decided the cases were loyal fascists, and no appeals could be taken from the verdicts handed down by the special courts The laws dealing with political crimes and treasonable activities were stated in vague and general terms so that almost any activity could be interpreted as an offense against the state Indeed, in Germany the special courts were able to punish acts deemed in conflict with the healthy sentiment of the people, even though the acts in question were not covered by any formal laws Individuals were punished for acts which were not crimes at the time when they were committed, since laws dealing with such matters were made retroactive sometimes, and individuals who could not be accused successfully of any crimes were often placed under police supervision, or "protective custody" The secret police apparently disposed of many cases without appeal to the courts, and millions of individuals languished in fascist concentration camps

*Lower Governmental Units* The powers of the fascist dictatorships extended, of course, to state (or provincial) and local governments, and these governments were converted into mere administrative agencies of the central government. Officials of state and local governments were appointed from above, legislatures or councils were eliminated or reduced to a purely advisory capacity, uniform national laws were passed in fields formerly reserved to the states or provinces, state or provincial constitutions were revised, and powers of state and local governments were transferred to the national government. National, state, and local civil services were combined into one uniform civil service, employees who were opposed to the state or politically undesirable (or, in Germany, non-Aryan) were removed from office, the traditional political neutrality of the civil service was eliminated, and all governmental employees were required to take an oath of loyalty to the dictator and be good fascists.

*Individual Rights* In strict accordance with the fascist political philosophy, the individual citizens of the fascist countries had virtually no rights. Since any criticism of, or opposition to, the policies or acts of the government or ruling party could be interpreted readily as treason, it is clear that freedom of speech did not exist. In a one-party dictatorship, with other political organizations strictly forbidden and with any non-party gathering of citizens likely to be regarded as subversive or treasonable, there was no freedom of assembly. Freedom of the press had also gone by the board. Each newspaper had to have a responsible editor (a synonym for fascist editor) and could not employ any journalists who were not approved by the government. The propaganda agency of the government rewrote the "news" and gave out rigid and elaborate instructions as to the manner in which important news items must be handled. In these ways, the newspapers were reduced to a "phonographic" level and the citizen had little reason for preferring one paper to another since they all dealt with the same topics in the same ways and were subject to ironclad censorship.

Education was also controlled firmly by the fascist dictatorships. The textbooks used in the schools were vehicles for instilling party propaganda in the youth of the land, and teachers suspected of having anti-fascist sympathies were ruthlessly weeded out. Contrary to the intention of schools in democratic countries, the fascist schools seemed to try to develop an inability to think on the part of the students, and a blind and unquestioning obedience to authority.

The principles of fascism were to be learned, not discussed or criticized, and "follow the leader" was a favorite pastime The job of the educational system was to make good fascists

School curricula were revised so as to place greatly increased emphasis on racial and political subjects and much less than formerly on languages, mathematics, and grammar Education at the high-school level was largely restricted to boys, and there was a tendency to train the "best" boys at party schools Even young men could not become college students unless they were "politically reliable," the heads of educational institutions were "trusted" individuals who held office by appointment from above, and it has been estimated that something like 60 per cent of the members of college faculties were replaced by party men<sup>14</sup>

The fascist attitude toward science and research was that they must be "coordinated" and made to serve the purposes of the state Scientists and research workers were instructed to give up their search for absolute truth and to learn to produce "fascist truth" Many scientists in the fascist countries were apparently coerced into prostituting their talents to the purposes of the state, and great masses of the most ridiculous party propaganda were thereby enabled to masquerade as bodies of scientific conclusions It was truly said that fascist propaganda knew neither right nor wrong, neither truth nor falsehood, but only what it wanted<sup>15</sup>

The fascist regimes differed somewhat in their attitude toward religion and the church The Catholic Church in Italy was very strong, and the treatment accorded it by the government was much less harsh than that meted out to their religious organizations by the Russian and German dictatorships In the early days of Italian Fascism, the church was more or less hostile to the regime but, in 1929, the government made certain concessions to the church and an armistice was arranged After 1929, a somewhat uneasy alliance existed between church and state

The Protestant churches of Germany had long been closely connected with the national government In the early days of National Socialism, they offered little opposition to the regime and even gave it some support However, the governmental decision to form a Union of Protestant Churches under a Reich Bishop and to give

<sup>14</sup> *Ibid.*, p 158

<sup>15</sup> R A Brady, *The Spirit and Structure of German Fascism* New York The Viking Press, 1937, p 31

the governmental Minister of Church Affairs rather complete sway over church matters led some prominent church men to revolt. These revolters were treated like any other political opponents of National Socialism. That is, they were forbidden to preach, use church property, or publish their opinions, their salaries were discontinued, and some of them were lodged in concentration camps. Relations between the German government and the Catholic Church were never too cordial after the rise of National Socialism and, in spite of an agreement which was reached in 1933, outright hostilities began in 1937. After that time many priests were tried and some convicted on charges of moral turpitude and the violation of currency regulations, and hundreds of them found their way to prisons and concentration camps. On the whole, it cannot be doubted that the National Socialists had very little use for religion.

The only individual right which survived for very long under fascism was the right to vote, and this right in Italy was limited to men and restricted by a variety of qualifications. German citizens 20 years of age or older, on the other hand, enjoyed universal, equal, secret, and direct suffrage. However, Jews or part Jews were not regarded as German citizens, while, by contrast, Germans who lived abroad were still considered as German citizens. Since the elections, when held, were most carefully controlled and farcical, and since very few offices were filled by election anyhow, the question of who had the right to vote was of comparatively slight importance. However, everyone who was eligible turned out to vote and voted as the party leaders desired, since to do otherwise might be considered to mean opposition to the fascist regime.

*The Program of Anti-Semitism.* The ordinary citizens of Germany may have been badly treated under National Socialism but their status was heavenly as compared with that of the unfortunate victims of the program of anti-Semitism. Jews were not allowed to hold public offices, own land, practice any profession, or own or work for any newspaper. It was extremely difficult for them to obtain an education. Jewish works of art and literature were destroyed and the playing of Jewish musical compositions was forbidden. Jews were deprived of their citizenship and political rights, required to carry identification cards, and made to give obviously Jewish first names to their children by adding Israel or Sara to their regular names. A persistent attempt was made to eliminate the Jews from the economic life of the nation and from all business.

pursuits. For this purpose a business was considered Jewish if one-fourth or more of its stock was owned by Jews, and it was a prison offense to conceal the Jewish character of a business. Jewish business owners were kept in durance vile in concentration camps until they became willing to abandon and sign away their wealth, or their businesses were restrained by heavy taxes, inability to secure materials, and other discriminatory practices until the owners became willing to sell out for a song to righteous Party men. German businesses were required to discharge their Jewish employees and Jewish workers were excluded from the Labor Front. All these activities were carried on with an intermittent accompaniment of slippings, beatings, and murders.

The prewar campaign against the Jews reached its peak in 1938, after a young Polish Jew in Paris killed an employee of the German legation. According to one source, the revenge for this act in Germany included the destruction of every Jewish shop and store, the dynamiting or burning of every Jewish synagogue, and the incarceration of 70,000 more Jews in concentration camps, while hundreds or thousands of Jews "committed suicide." The Jews were required to pay for the damage which had been done, since any insurance benefits which they could collect were forfeited to the state. In addition, the Jews were required to pay a fine of a billion marks, and they had to sell much of their remaining wealth at ridiculously low prices in order to do so.<sup>16</sup>

The purposes behind the program of anti-Semitism in Germany were quite easy to ascertain. No one outside Germany took much stock in the National Socialist doctrine of racial superiority. While many Germans have blue eyes and blond hair, most people who understand such matters regard the Nordic or Aryan race as a pure myth, and anyone could be greatly amused when the National Socialists began to rave about Italian Nordics or Japanese Nordics. The real reasons behind the anti-Jewish campaign seemed to be two in number. In the first place, the Jews furnished the National Socialists with a scapegoat or bogeyman on which all misfortunes, domestic or international, could be blamed. Thus, the Jews were blamed for the loss of World War I and for the widely known abuses or bad features of capitalism, such as profiteering or unemployment. They were charged with responsibility for the existence of Communism, Bolshevism, class war, trade union activities, and

<sup>16</sup> K. Leowenstein, *Hitler's Germany*, pp. 107-116.

internationalism Even World War II was blamed on the "iniquities of Jewish international bankers" Obviously, the chastisement of such a scapegoat might help to distract the attention of the people from their own immediate woes and frustrations The second reason was even more practical It was thought that the elimination of the Jews would give jobs to deserving Germans in general and Party men in particular, and that Jewish wealth could be transferred to other hands with the transactions disguised in a righteous crusade During World War II, the campaign against the Jews knew no bounds Millions of these unfortunate people, both in Germany and in countries overrun by the German armed forces, were killed by means of a variety of devices whose fiendish ingenuity almost baffled the imagination, and those who were lucky enough to escape with their lives usually were able to salvage little else

### *The Fascist Parties*

**The Party and the Government** As we have seen, the fascist political parties (National Socialist in Germany and Fascist in Italy) were in complete and absolute control of the government Virtually all governmental offices were filled by loyal party men, who usually received their positions by appointment rather than by election and held office for indefinite periods, set by their superiors In both countries, moreover, the outright control of the government by the party rested upon an official and legal basis In Germany, this basis was composed of the emergency decree of von Hindenburg in February, 1933, the law of July, 1933, which declared the National Socialist Party to be the only one with the right to exist in Germany and made the formation of new political parties or the reconstitution of dissolved political parties a treasonable offense, and the law of December, 1933, which made the National Socialist Party officially a part of the government of Germany In Italy, the Party's Grand Council became an organ of the state and was assigned the duty of preparing electoral lists in 1928, the internal organization and discipline of the party were prescribed by law after 1929, the national secretary of the party was appointed by royal decree and had the rank of Minister after 1937, and the constitution of the party was established by successive governmental decrees

**Party Organization** Both fascist parties had very elaborate in-

ternal organizations In Germany, the organization proceeded from local groups and leaders through county and district groups and leaders up to the Central Directorate of the party and the great dictator himself The party controlled the activities of a variety of structural groups which included the *Sturmabteilung* (Storm Troopers), *Schutzstaffel* (Elite Guard), the Hitler Youth Organizations, the National Socialist Motor Corps, the National Socialist Students Association, and the National Socialist Women's Organization The Storm Troopers were not necessarily members of the party, since it was originally the intent of the party to keep certain undesirable elements out of the party proper even though they might be good enough to do the "rough" work Almost any able-bodied man could join the Storm Troopers The Elite Guard, on the other hand, admitted only Party men with perfect political records and high physical qualifications In addition to the structural groups, there were nine associations affiliated with the party, including those for doctors, lawyers, teachers, technicians, public officials, university teachers, and the Labor Front

In Italy, the party structure was based on some 10,000 local chapters (*fasci di combattimento*), which were grouped into 94 provincial federations, each with a secretary nominated by the national secretary and appointed by Mussolini Further up there were other agencies and officials, crowned by the national party secretary, a National Directorate of 13 members, the Grand Council of the Party, and finally the leader, Mussolini himself As in the case of Germany, there were numerous other organizations affiliated with the Party

Both fascist parties, like the Communist Party in Russia, maintained an organization of their own parallel to, although strictly separate from, the apparatus of the state That is, there were party officials and agencies to correspond to the various officials and agencies of the government As in Russia, the same men often held both the party offices and the corresponding governmental offices, though they might be served by different staffs in each capacity In the fascist parties, as in the government, power was greatly concentrated at the top The leaders made all the important decisions and there was really no such thing as control or even effective discussion from below

*Party Membership* While large numbers of people in both countries were affiliated with some party organization or other, member-

ship in the party proper was limited to a small minority of the population, or about 4,000,000 persons in Germany and 2,500,000 to 3,000,000 in Italy.<sup>17</sup> Party membership was eagerly sought after and carried with it both prestige and possible economic gains in the form of employment, wealth, and income. Candidates for party membership had to take an oath of blind loyalty, undying devotion, and unquestioning obedience to the dictator. Members had to place themselves and their resources at the disposal of the party and were subject to strict discipline on the basis of a party code which specified the pattern of their behavior. The qualifications of party members were reexamined at relatively frequent intervals, and undesirable members were purged from the party, if not from this world.

*Party Youth Organizations* Both parties were closed to new adult members from time to time and, in general, believed in obtaining their new members from the party youth organizations, which took over the lives of boys and girls at an early age and subjected them to intensive training for citizenship and party membership and affairs. Both parties had elaborate systems of youth organizations, with a membership double or more than that of the party itself, but details of these organizations need not concern us. The boys were instructed in party principles, taught obedience and loyalty, given quasi-military training and physical culture activities, and in general were brought up to be good fascists. The girls were taught that woman's place is distinctly in the home, surrounded preferably by large numbers of growing young fascists.

### *Similarity of German, Italian, and Russian Governments*

We should not leave the subject of government without reminding ourselves of the great similarities which have existed between the governments of Soviet Russia, Italy, and Germany. Among the many common features we may list the following: (1) strong dictatorship with great concentration of power in the hands of one man, (2) a one-party system of government, with party members holding all or most important positions, with complete party control over the government, and with party officials and agencies to match those of the government, (3) figurehead legislative and judicial de-

<sup>17</sup> *Ibid.*, p. 72, and *Statesmen's Year Book*, 1941, p. 1041.

partments, (4) strong control by the national government over "state" and local governments, (5) the practice of filling many important governmental offices by appointment rather than by election, (6) ruthless and thorough methods of subduing the opposition to the existing regime, special treatment and severe punishments for political crimes, and the maintenance of a large and efficient secret police operating at least partly outside the laws and forms of government, (7) the practice of getting all eligible citizens to vote and vote right, while other rights of individuals are suppressed, and (8) the requirements for party membership, the closing of the party to new adult members, the frequent reexaminations and purges of membership, the desire of the people for party membership, and the extensive and elaborate party youth organizations. These matters could be boiled down to a smaller number of points or they could be stretched out to make a great many items, but they present a picture of the striking similarities which have existed among these three governments.

On the other hand, the *number* of differences between the governments may be even larger. One government has a democratic constitution while another did not or had none at all, one government retained its former nominal head while another has dispensed with the office in question, one dictator might hold several cabinet positions, a second only one, and a third none at all; and so on. Without enumerating any more of these differences, we may say that, on the whole, they seem relatively trivial and unimportant in comparison with the similarities. On the basis of the similarities in the matter of government, many people in the United States came to the conclusion that the Communist, Fascist, and National Socialist systems were identical, or nearly so, in all other respects. Whether this conclusion was justified in connection with the economic organizations and policies of the various systems will be seen in the chapters which follow.

#### QUESTIONS

- 1 Why do most people regard the government of Britain as democratic?
- 2 Compare the British legislature with that of the federal government of the United States.
- 3 "The nature and functions of the Cabinet in the British government are almost exactly the same as those of the Cabinet in the government of the United States." Do you agree? Explain.

4. "The rights of British citizens are the same as those of citizens of the United States, but they rest on a different basis" Explain
5. "Britain is likely to be the first country to have socialism in economic matters and democracy in government at the same time" Show whether you agree
6. Describe the development of the Fascist movement in Italy after World War I
7. "The condition of Germany in the first few years after World War I was even worse, if possible, than that of Italy" Explain
8. Describe the various factors which were responsible for the rapid growth of the National Socialist Party in Germany after 1928
9. How did the fascist notion of the relationship of the individual to the state differ from that which is widely held in capitalistic countries?
10. "The fascist philosophy was anti democratic and anti-socialistic" Explain
11. "Fascism involved only a change in the control over existing governmental mechanisms rather than a modification of these mechanisms" Discuss
12. How were the nature and functions of the national legislatures modified under fascism?
13. What happened to the court systems under fascism in Italy and Germany?
14. Why were the fascist governments of Italy and Germany called dictatorships by outside observers? Explain
15. "The dictatorial powers of the fascist governments extended to virtually all phases of national life" Explain
16. Indicate the purposes and methods of the fascist program of anti-Semitism in Germany
17. "The fascist parties in Italy and Germany were strikingly similar to the Communist Party in Soviet Russia" Explain
18. "The governments of Soviet Russia, Italy, and Germany had many important common features as long as the latter two countries were under fascist regimes" Show whether you agree
19. How did the governments of the fascist countries differ from that of the United States during World War II? Discuss

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## CHAPTER 5

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### *MAKING ECONOMIC DECISIONS*

HOWEVER much economic systems may differ with respect to such matters as economic institutions and government, the general nature of the economic problem is the same in all systems. And in every economic system certain basic economic decisions must be made. In some manner or other, it is necessary in every economic system to determine (1) the kinds and quantities of various economic goods which are to be produced, (2) the way in which the various productive agents are to be allocated or distributed among the many industries and fields of productive activity, (3) the manner in which the immediately available stocks of consumers' goods are to be distributed among consumers, and (4) the total quantity of each reproductive agent of production which is to be available in the long run. As we shall see, decisions on these points may be reached in different ways in different economic systems. Under capitalism, they depend very largely on price relationships, and the reactions of individuals and enterprises to these price relationships. Thus, the price system is an institution which is fundamental to the operation of a capitalistic economy.

#### *Making Economic Decisions under Capitalism*

**The Control of Production** A capitalistic system has no dictator or all-powerful planning agency to specify which economic goods may be produced and which may not, or to determine the relative quantities of various economic goods which should be produced. By and large, the individual is left free to produce any goods which he selects and in any quantity which seems appropriate to him, while the total decisions as to the kinds and quantities of economic goods to be produced are merely the aggregate of the decisions of individual enterprisers—decisions made on the basis of price rela-

tionships If consumers desire very strongly a certain economic good, such as electric refrigerators, and the quantities which are currently being produced and sold are small relative to the effective demand, we may expect that the prices of electric refrigerators, at least in the shorter periods of price determination, will exceed their production costs per unit Such a favorable price-cost relationship will ordinarily induce the manufacturers of electric refrigerators to produce more of them and may eventually tempt the manufacturers to expand their plant and equipment so that they can continue to increase production Again, the favorable price-cost relationship is likely to attract new enterprisers to the industry and it will enable the enterprisers, both old and new, to bid effectively for land, labor, and capital, so that necessary additional amounts of these productive agents may be secured and utilized for the production of electric refrigerators In the long run, under competition, the tendency is for the production of electric refrigerators (or other economic goods) to become adjusted to the relative strength of the demand for the goods on the part of consumers

Adjustments in the other direction are produced in similar fashion If more victrolas are currently being produced than consumers desire to purchase at the going price, the price may fall until it is well below the level of cost of production per unit Such an unfavorable price-cost relationship will usually lead enterprisers to restrict production and it may eventually cause some enterprisers to leave the industry altogether Moreover, it will become difficult for enterprisers to attract additional quantities of the productive agents to their industry or even to retain the quantities which they already have The process of adjustment will end only when the productive capacity and output of the industry producing victrolas have once more been coordinated with the relative strength of the effective demand for the product on the part of consumers

Thus, it has been said that

Under capitalism, it is profit making, not love, that makes the world go round For it is the expectation of profit which induces those who own the means of production to permit them to be used But profit making is not only the incentive, it is also the regulator of capitalist production Under capitalism it is not only the object, it is the very condition of production that a profit should result Those things, that is to say, which will yield a profit can and will be produced, *but those things alone* For anybody who produces things which do not, either directly or indirectly, yield a profit will sooner or later go bankrupt; lose his ownership of the

means of production, and so cease to be an independent producer Capitalism, in other words, uses profitability as the criterion or test of whether any given thing should or should not be produced, and, if so, how much of it should be produced

Now the test of profitability ensures that those things, and only those things, for which there is a demand shall be produced Profit is, as it were, a magnet which draws production after demand For it is profitable to produce those things for which there is a demand, and unprofitable to produce those things for which there is no demand But things are not either in demand or not in demand The demand for them varies in strength Under capitalism it will be profitable to produce more and more of those things for which there is an increasing demand, and less and less of those things for which there is a decreasing demand Thus, our productive resources are continually being pulled by the magnet of profit toward the production of those things for which there is an increasing demand, and away from the production of those things for which there is a diminishing demand<sup>1</sup>

The net result of the system is apparently that just those economic goods which most people want most strongly, and no others, will be produced

*The Allocation of the Agents of Production* As the discussion of the control of production has implied, productive agents are, in general, allocated or distributed among enterprises and industries on the basis of prices under capitalism We are not here discussing the production of *additional units* of reproducible productive agents on the basis of a favorable relationship between the cost of producing the agents and the prices which can be obtained for their use, but rather the way in which *available quantities* of productive agents are distributed among firms and industries When a piece of land in an urban area becomes vacated and a new tenant or purchaser is sought, the question as to whether the land should be used as a site for a department store, garage, residence, manufacturing plant, theater, or hotel will ordinarily be answered on the basis of the prices which enterprisers of these various kinds are willing to pay for the land or the rents which they are willing to pay for its use Other things being equal, the owner of the land will probably turn it over to the enterprise or industry which is willing to pay the highest price for it or the highest rent for its use In the long run, the entire supply of land tends to be distributed in similar fashion on the basis of the prices which enterprises and industries

<sup>1</sup> John Strachey, *How Socialism Works*, pp. 16-17 Reprinted by permission of the author

are able and willing to pay for it or its use. No conscious attempt is usually made to see that the available quantity of land is awarded to those firms or industries whose operation is most necessary to the social welfare. Rather, it is generally assumed, from the social point of view, that those industries which can pay most for the land are those which should get it.

When quantities of capital funds are available for investment, the question as to whether they should be used to provide capital goods for automobile production, or facilities for the production of shoes, housing, ice cream, or something else will usually be decided on the basis of the amounts of interest which firms in these various fields of production are able and willing to pay for the use of the funds, due allowance being made for risk in each case. It is only rarely that an owner of capital funds will turn down a safe and attractive rate of interest because he does not approve of a product or the business policies of the firm which offers it, or for any other reason. Even capital goods themselves, to the extent that they are mobile and are capable of being used in different types of productive activity, will ordinarily be turned over to the enterprise which can offer most for their use.

Finally, it should be said that available units of labor also tend to distribute themselves at least in part on the basis of the prices which are obtainable for their services in various occupations and industries. This is not to say that the worker, in considering the desirability of shifting from one occupation to another, will be exclusively influenced by the money wages which are obtainable. He will also give attention to such matters as the pleasantness or unpleasantness of the two occupations, the risk or danger involved in each, the relative prospects of advancement, and the probable steadiness of employment. However, workers do shift from one occupation to another, and the principal reason for these changes, although not the only reason, is the desire for high rather than low wages. Many industries which now employ large numbers of workers, such as those producing automobiles, radios, airplanes, and air-conditioning equipment, did not even exist years ago, and they have been able to attract their labor supplies largely because they could offer workers higher wages and better conditions of employment than other industries.

*The Apportionment of Consumers' Goods.* Economic goods command a price because they are scarce in relation to the desires of

people for them Since there are never enough consumers' goods to satisfy all wants or to permit consumers to help themselves freely to the goods, some method or other must be found of apportioning the available supplies of consumers' goods among the people who want them or of holding down the buyers to a number who can satisfy their wants from existing stocks of goods Under capitalism, the rationing of consumers' goods among the persons who desire them is also ordinarily accomplished on the basis of prices If the available stock of potatoes is unusually small, a continuation of the old price would cause the sellers to be swamped with prospective buyers, but, if the price is raised sufficiently, the number of buyers will be restricted so that the market demand for and market supply of potatoes will be in equilibrium once more If the available stock of oranges is unusually large in relation to market demand at a high price, the continued charging of a high price would result in the piling up of large quantities of unsold oranges, but, if the price is lowered sufficiently, the number of buyers who come forward may be increased until the quantity of oranges which sellers desire to sell is exactly equal to the quantity which buyers are willing to purchase It is only in the face of great emergencies, (as, for example, in wartime) that a capitalistic economy will attempt to control prices and resort to the rationing of consumers' goods by quantities instead of relying on price movements to equilibrate market demands and market supplies

*Controlling Total Amounts of Productive Agents* Finally, it is also true that price relationships control, where possible, the total amounts of agents of production which will be in existence in the long run That is, a high rate of remuneration for such an agent of production leads to an increase in its amount, while a low payment leads to a decrease in its quantity However, it is not always possible to create more of an agent of production In the case of land, it is clear that rents and land prices may go up indefinitely without bringing about any increase in the quantity of natural things The case of labor is not so clear as that of land The total number of workers available for production may be increased or decreased through time, but it is difficult to estimate the extent to which the number of workers is dependent in the long run upon the wages paid for labor In spite of the various theories which economists have developed from time to time connecting population growth and hence labor supply directly or indirectly with wages, the best

conclusion seems to be that increases in population and the labor supply occur because of a great number of factors—not all of which are economic in character by any means—and that it is virtually impossible to single out any one factor, such as wage rates, and estimate its effect on population and labor supply.

Capital, therefore, seems to be the productive agent whose total quantity is most responsive to changes in price relationships, although the savings which are necessary for capital formation depend upon a number of factors besides the desire to receive interest. Saving occurs, for example, because individuals wish to provide for their own old age or for their heirs, because they want to keep a reserve on hand against the various financial emergencies which may arise suddenly, because they wish to acquire power or prestige, or because they have such large money incomes that they are unable to contrive ways of spending their entire incomes on their personal needs and desires. These factors indicate only that some saving would occur even if interest were not paid, they do not show that the total quantity of savings would remain unchanged if interest were abolished. There are many units of individual income which are just about on the margin of being saved or not being saved. An increase in the rate of interest will ordinarily cause the owners of such marginal units to forego present consumption and save larger amounts out of their money incomes, while a decrease in the prevailing rate of interest will result in the spending of more of these units of income for current consumption and the saving of fewer units than formerly.

Thus, not all units of savings need be directly dependent upon the size of the prevailing interest rate in order that a change in this interest rate may bring about a change in the total quantity of saving and capital formation. The chances are that an increase in the interest rate, other things being equal, will sooner or later bring about an increase in the total quantity of capital funds at the disposal of society, while a decrease in the interest rate will eventually cause a decrease in the total quantity of capital funds available for use in production. The magnitude of the total supply of capital funds, as well as the distribution of the existing quantity among industries, tends to depend upon price relationships.

*Theoretical Results* It is faintly clear that the full working out of all the tendencies which we have been describing would result in complete economic equilibrium on the basis of price relationships,

but some people would go so far as to allege that such an equilibrium would also be an economic optimum and would result in the maximization of economic and social welfare for the citizens of the economy. As the result of the control of production on the basis of price relationships, only those goods will be produced by the members of society as producers which the members of society as consumers desire, and the relative quantities of the various economic goods produced will be adjusted to the demands of consumers for them. The production of each economic good will then be called to the point where the last unit produced will command a price sufficient, and only just sufficient, to cover the cost and effort of producing it, at the same time, the consumption of each economic good will be carried to the point where the last unit purchased is expected to produce a degree of satisfaction which is sufficient, and only just sufficient, to justify the price paid for it. Since at this margin both expected satisfaction on the one hand and cost or effort on the other are supposed to be equal to the same thing (the price of the good), it is customary to assert that they are equal to each other. But, because other units of the good before the margin is reached are expected to give more satisfaction than the marginal unit and are expected to cost less than the marginal unit, ideally the industry which produces that particular good, and hence all industries, will control production so that they furnish society with the greatest possible surplus of satisfactions over efforts or costs.

If the agents of production are allocated among firms and industries strictly on the basis of prices, their employment will be perfectly coordinated with the desires of consumers as expressed on the market. No unit of any productive agent will be used for the production of a particular economic good if its use in the production of some other economic good would result in a greater-value product or a higher rate of remuneration for the owner of the agent. Because of the apportionment of finished goods and services among consumers on the basis of prices, no unit of any economic good would be purchased and consumed by a particular person if a greater marginal utility would result from its purchase and consumption by someone else (in so far as marginal utilities are accurately measured by the willingness of individuals to pay prices on the market). Finally, in the state of full equilibrium on the basis of price relationships, the productive resources of the economy would be divided between providing for the present (through the production of fin-

ished commodities and services) and providing for the future (through capital formation) in perfect accordance with the time preference and desires of the citizens Such is the glittering prospectus which may be offered in connection with the operation of the price system and its results

*Obstacles to Equilibrium* However, the price system does not perform its functions (or rather individuals do not function on the basis of price relationships) as efficiently in practice as in theory The theoretical description of the operation of the price system assumes, explicitly or implicitly, the existence of certain conditions which are only roughly approximated in the operation of an actual capitalistic economy These assumptions include conditions of competition (as previously defined), the complete mobility of the productive agents as between industries and places, and lack of governmental interference with the processes of the market When these conditions are imperfectly realized, the results produced by the operation of the actual price system do not conform closely to those of the theoretical model

In actual practice, the agents of production are never completely mobile Once land has been committed to a particular enterprise or industry, it is ordinarily tied up for a considerable period of time and cannot be shifted at once to other enterprises or industries even though more profitable opportunities for its employment arise In similar fashion, when capital funds have actually been invested in fixed plant and equipment in some industry or other, and these capital goods will last for a number of years, a change in price relationships which would make it possible for these funds to earn more interest in some other type of investment will not cause the funds to move at once to another industry Hence, in the shorter periods of time, a large part of the economy's capital funds is likely to be immobile, and we cannot expect to find the distribution of the funds among industries to be perfectly suited to the price relationships which exist at a given time However, it remains true that, in the long run, all capital funds are mobile and none are tied up in fixed capital goods If savings will command more net interest in some uses of funds than in others, or in some places than in others, after allowing for risk and costs of administration, it is to be expected that, in general, savings will move *in the long run* from occupations or places where net interest is low to occupations or places where net interest is high That is, as capital goods wear out

and create funds for their replacement, these funds will be transferred to another occupation or place instead of being reinvested in new capital goods of the original type.

It must be admitted that price relationships operate less effectively in distributing workers among industries than in distributing land or capital funds. The fact that the wages of scrub-women are very low in relation to those of opera singers will not cause the former workers to throw away their pails and mops and mob the opera houses, nor will the fact that college professors are better paid than street-car motormen cause the latter workers to attempt a mass invasion of the ivory towers of learning. The simple fact is that the labor supply does not consist of a single large mass of like units of labor, all of which engage in competition for the entire range of available jobs. Instead, because the labor supply is stratified into various groups or grades of labor, the members of one group find it most difficult, if not impossible, to compete for the jobs which are open to the members of a higher group. The nature of these labor groups (such as unskilled, semi-skilled, skilled, and professional and managerial labor) and of the hereditary and environmental obstacles to movement from a given group to a higher one will be familiar to most readers.

Even if we limit the discussion to the various occupations which are open to the members of a single labor group or grade, we find that workers do not always shift occupations in response to changing wage rates. In some cases, of course, workers may continue to accept a certain wage, even though a higher one is available in some other occupation, because they are not aware of the various opportunities which exist for their employment or because their movement is prevented by powerful unions. In other cases, they may know of the higher wage rates to be obtained in other occupations and may be qualified for these other jobs, only to be unable or unwilling to take them because the better-paying jobs are out of commuting distance. The workers may be unable to afford the expense of moving themselves and their families to another place, they may have formed an attachment for their present location, they may have children in school whose opportunities for education would suffer in the new community, or they may have homes of which they could not dispose without incurring a considerable loss.

Thus, the distribution of the agents of production among industries and places on the basis of prices is not an accomplished fact.

under capitalism but merely a tendency which operates slowly and haltingly through time. The relative immobility of the agents of production obviously has an important effect upon the success with which production can be controlled on the basis of price relationships. Favorable or unfavorable price-cost relationships do afford a stimulus to the expansion or contraction of the production of particular economic goods, but adjustments of production to changes in demand cannot occur quickly and smoothly because of the immobility of the factors of production. And, all too often, before an adjustment of production to one change in demand can be completed, another change in demand will occur which will render the attempted adjustment of production inappropriate.

The market conditions which prevail on the supply side of price determination are also important. It is only under competition that the enterprisers in any particular industry, in reacting to increased demand and favorable prices, may be expected to expand production so much that the price of the product will necessarily fall back to the cost of production level. In controlling the affairs of their enterprises, monopolists and monopolistic competitors must pay attention to the demand for their products, but under any given demand they have no incentive to carry production to the point at which they can obtain prices which will only cover the average cost of production per unit of their goods. Instead, they tend, under any given conditions of demand and productive capacity, to limit output to the volume at which the marginal cost of producing the good is equal to the marginal revenue derived from its sale. Since such an output is ordinarily well short of that at which price just covers average cost of production per unit, it follows that the productive results of operation under conditions of monopoly or monopolistic competition are quite different from those envisaged by the general description of the control of production on the basis of price relationships. In somewhat similar fashion, the existence of conditions of monopoly or semi-monopoly on the demand or supply side of the markets for factors of production, or even the existence of conditions of monopolistic competition in the sale of products whose producers are also, of course, demanders of the productive agents, will have an influence on the prices at which the total available stocks of productive agents can find employment, on the distribution of the agents among industries, and on the kinds and relative quan-

tities of economic goods which the entire economic system will produce

Under conditions of monopolistic competition, products are differentiated and the individual enterprise is in a position to control the market for his product to some extent. In such a situation, the enterprise may readily decide that it will be better for him to try to "educate" the consumers to want what it seems appropriate for him to produce than to try to suit his product to the supposed wants of consumers. The simple theoretical discussion of the control of production on the basis of price relationships tends to overlook the whole range of advertising and other economic activities whose purpose is, at least in part, to change the pattern of human wants rather than to satisfy the wants which already exist.

Governmental interference with and control of economic activity may alter considerably the total productive and other results achieved by a capitalistic economy. Even in an economic system which is ostensibly capitalistic, governmental action may forbid altogether the production and sale of some commodities and services, may regulate the production and sale of other economic goods, may interfere with the ordinary bargaining processes of labor markets by sponsoring and encouraging labor organizations, and may establish minimum wages and maximum hours for workers—to mention only a few things. After governmental interference and control is an established fact, the productive and distributive processes of the economy will undoubtedly adjust themselves again on the basis of price relationships in the new situation, but the total results achieved will never quite be what they would have been in the absence of governmental intervention.

The method of apportioning consumers' goods among the persons who desire them by means of price changes, or of bringing the market demands for and market supplies of economic goods into adjustment by means of price changes, is capable of working very efficiently. There is always a price high or low enough to move any quantity of an economic good, however large or small, off the market. In actual practice, however, the method works much better in one direction than in the other. When certain economic goods are unusually scarce, prices ordinarily rise readily, and the numbers of buyers or the quantities demanded are restricted. When economic goods exist in quantities which cannot be disposed of at the prevailing prices, the prices do not always fall readily, and we some-

times see large unsold stocks of these goods piling up while many people desire to purchase them and cannot do so. The difficulty here is not that the price mechanism will not work but rather that producers and sellers do not care to let it work. That is, they are unwilling to lower prices to levels at which all the available goods could be sold.

The method of controlling long-run supplies of productive agents by means of prices applies with real force only to capital, and even here the results produced are far from perfect. The total quantity of savings and of capital often adjusts itself very slowly to changes in the interest rate. In times of depression saving may go on at a considerable rate even though the rate of interest has been declining steadily and the demand for funds to invest in industry is light. On the other hand, in highly prosperous times the demand for savings to invest in productive facilities may outrun the total quantity of savings although the rate of interest rises considerably.

*Equilibrium and Economic Optimum* We see then that, while there are forces making for equilibrium in the operation of a capitalistic economy on the basis of price relationships, full economic equilibrium is not likely to be completely worked out at any particular time. And even if full economic equilibrium did exist in practice, there would still be several reasons for doubting whether this result would be an economic optimum or would mean the maximization of economic and social welfare. In the first place, it is clear that the control of production through changing price relationships merely adjusts production, at best, to the effective demands for goods in the market, and not to basic human desires or needs. Production would be adjusted to human desires or needs only if all persons demanding economic goods had substantially equal money incomes (and perhaps not even then). Under this condition, consumers would presumably offer highest prices for the goods which they desired most. Thus the existence of a high price for a good would indicate a strong consumer desire for more of it, while low prices would prevail for unimportant goods or goods the demands for which were already being relatively well satisfied. Under the actual conditions which prevail under capitalism, with great inequality in the distribution of money income among individuals, the reliability of these price indications is partly destroyed. A high price may prevail either for an essential good which is in strong demand or for some trivial, unimportant good whose purchasers have a

great deal of money to spend. Similarly, a low price for a good may mean that the good is of little importance and that the demand for it is already well provided for, or it may mean that the good is one of considerable importance, perhaps even a necessity of life, but that those who would ordinarily purchase it have little money to spend for it or for anything else.

Business enterprisers, who are on the lookout for goods whose prices are favorable in relation to their costs, do not bother to ask *why* the prices are what they are. Indeed, it would be too much to expect them to investigate the reasons why people demand the goods which they do, in fact, demand. Thus, under capitalism, with its inequality in income distribution, the reaction of enterprisers to price relationships alone serves to direct agents of production into the production of nonessential goods while really important human wants go at least partly unsatisfied. It leads to the production of yachts for the transportation of the few before there are enough shoes for the transportation of the many and to the production of cake for the rich before the needs of many poor people for bread are satisfied. Under conditions of extreme inequality in the distribution of money income, even the most perfect adjustment of production on the basis of price relationships could scarcely be considered to produce an economic optimum.

On the other hand, we should not be on secure ground in asserting that perfect equality in the distribution of income and wealth would be necessary to the existence of the economic optimum. We have no way to make objective comparisons of satisfactions or utilities as between persons and there is no way to measure aggregate satisfactions for the whole population of the economy because of possible differences between individuals with regard to their capacities to experience satisfactions. Certainly the common assumption that all persons have equal capacities for satisfaction is incapable of scientific proof. Thus, apart from any questions of the distribution of money income, we need to know more about the psychological basis of human wants before we decide that a given equilibrium condition would be an economic optimum. To what extent is it possible for prices to measure the strength or magnitude of basic human needs or wants? The economist's understanding of the psychological basis of human wants is none too strong and the usual utility analysis is rather unsatisfactory from the point of view of psychology. When we say that an individual wants a good be-

cause it has utility for him, all we are really saying is that the individual wants the good. Until we have a more complete knowledge of human motivation, we are not justified in saying that full economic equilibrium on the basis of price relationships, even if it resulted in the equalization of marginal "utilities" or marginal "desires," would be an economic optimum.

In the second place, we note that the market and price mechanism does not furnish us with a satisfactory means of expressing all our wants. It would be possible, we may suppose, to allow private enterprisers to furnish us with such things as fire protection, education, and health service on the basis of price relationships, but we do not do so. Because of the great importance which we attach to these services and because of our complete unwillingness to accept as appropriate the volumes of them which would be provided for us on the basis of price-cost relationships in the market, we insist that the provision of these services be taken out of the realm of the market and that it be undertaken by public authority. Again, some of our more complex wants seem to baffle the ingenuity of the market and price mechanism altogether. Take, for example, the matter of national defense, or the protection of the citizens of the economy from attack by external enemies. As Mrs. Wootton has said, "No device readily suggests itself by which such of the inhabitants of a given territory as were unwilling to subscribe to the cost of maintaining an army could be prevented from enjoying its protection in time of war, or, which would adjust the amount of protection enjoyed by each citizen accurately to the amount that he chose to spend upon this service."<sup>2</sup> Or, consider the desire for economic security, which undoubtedly holds a high position in the valuation scales of many individuals. Clearly, "There is no way in which we can go into the market and, as it were, bid up the value of security, so as to stimulate the economic system to deliver more of this admirable product."<sup>3</sup> As a final example, suppose we have a desire to live in an economy which is marked by much less inequality in the distribution of income than is our own capitalistic system. There is apparently no way in which our willingness to pay prices of any magnitude in the market can lead to the satisfaction of this desire.

<sup>2</sup> Barbara Wootton, *Lament for Economics*. New York: Farrar and Rinehart, Inc., 1938, p. 177. Reprinted by permission of the publishers.

<sup>3</sup> *Ibid.*, p. 202. Reprinted by permission of the publishers.

Thirdly, the market and price mechanism, as such, gives consumers no opportunity to bid against the production and sale of certain commodities and services which they regard as undesirable. There may be a great many people whose total of satisfactions would be much increased if they could prevent the publication and sale of a particular book or the production and sale of alcoholic beverages, noxious patent medicines, or other products, and who would be glad to pay prices to obtain such satisfaction of their negative preferences if any opportunity could be given them to do so. But there seems to be no way in which the market mechanism can take these negative preferences into account, and we may exercise these preferences, if at all, only by public (that is, governmental) action.

Finally, the market mechanism provides no means for measuring the efficiency with which the market mechanism works or the total satisfaction which is derived from its use in comparison with that which might be realized from the use of some alternative mechanism for the allocation of scarce means among alternative ends. The defense of the market mechanism in these connections is usually stated in terms of the freedom of choice which this mechanism affords to consumers in the capitalistic system. However, on examination, we might well find that the freedom of choice which consumers would really like to have would be at the same time more comprehensive and less detailed than that which the market mechanism actually offers. It would be more comprehensive because, in actual practice, the consumers' choice as to the various uses to which the productive resources of the economy should be put is secondary rather than primary. That is, the market and price mechanism never asks the consumers to specify the various commodities and services for the production of which they would like to see the scarce resources of society used. The really fundamental choices are made by business enterprisers, who decide what commodities and services should be placed on the market, and consumers can actually choose only among the various options which are offered to them by the enterprisers.

The ideal freedom of consumers' choice would be less detailed than that which they actually have because, "As a matter of actual experience, there is indeed quite a good case to be made for the view that the market, in modern conditions, imposes upon consumers, or at least upon those of them who are even moderately affluent, a range of choice which is actually burdensome. On the

theory that I alone know what is satisfying to me, the market insists upon offering me a bewildering variety of alternatives from which to choose. The business of selecting between scores of varieties of cosmetics or saucepans or neckties is really very arduous, and one of which many of us would gladly be in large measure relieved. And, moreover, it is a business which most of us, most of the time, are quite incapable of conducting intelligently. True consumer's choice, with its implication of *caveat emptor*—let the buyer beware—is all very well in a society in which consumers are in general equipped at least with the minimum of technical knowledge necessary for enlightened choice. Today, as everyone knows, they are mostly very far indeed from being in this happy state. As a purchaser of jams, for example, I am quite incapable of deciding for myself which varieties are made of fruit and which are synthetic substitutes, nor do I even know, at all accurately, how far the substitutes are, on the one hand, actively pernicious, or on the other hand, just as good as the commodity which they replace. As a purchaser of textile goods, again, I am quite incapable of discriminating between weight which is due to the quality of the material and will promote hard wearing, and the specious heaviness which is achieved by excessive loading or dressing, and which will disappear the first time that the stuff is washed or cleaned. I may, perhaps, claim to be a discriminating purchaser (discriminating, that is, of course, in terms of my own standards of satisfaction) of books on economic or sociological topics, but few of us can claim such competence in more than one or two fields. Even where we do realize our own wants and would value the power to direct resources to their satisfaction, this very readiness to exercise choice is, in fact, over and over again doomed to sterility, just because we are pathetically incapable of recognizing whether what we get is, or is not, what we wanted.

Nor is it any answer to say that in a competitive world, we can profit both by our own mistakes and by those of others, so that the more satisfying product will always, in the long run, win over the less. For, in the first place, this is an expensive and tedious way of correcting a distribution of resources which the public does not find satisfying. It is indeed true that those who have purchased material that dissolves in the wash may be to some extent forearmed next time (though, if they are still technically ignorant, even bitter experience will not be an infallible defense against a repetition of the tragedy), and true also that, in time, the boycott of an unsatisfactory product by those who have discovered its shortcomings may make its sale so unprofitable that its production is

discontinued, with the result that others are spared a like experience. But this does not alter the fact that the consumer's freedom of choice would have meant a great deal more to him if he had been able to detect the faulty product *before* he had elected to buy it. And, in the second place, while suspecting that some of our choices are unsatisfactory somewhere, we may never be able, even after experience, to lay our fingers on the exact spot where we went wrong. I want to buy good food, and I know that I may make myself and my family ill, if I fail to do so, but I may well be far too ignorant to locate just where my buying is at fault, even when I perceive that I am not getting satisfactory results.

In view of these familiar facts it is, I suggest, quite absurd to suppose that market demand can claim, even under competition, faithfully to direct resources into production of just those things that are wanted in any commonsense meaning of the word, or even to do this job so well that no alternative is worth looking at. It is far from self-evident that it would not be better, for example, in some cases to consult the consumer as to the general outline of the pattern of production, and then settle details over his head, as a planned economic system, conducted in a politically democratic society, but not pledged rigidly to follow the lead of the market, might do.<sup>4</sup>

After considering all these factors, we may well decide, as many other economists have done, that, even if full equilibrium on the basis of price relationships could be achieved under capitalism, it would be just equilibrium and nothing more. Or, if we are determined that such an equilibrium must be an economic optimum of some sort, we should consider it only as a practical optimum, rather than an "optimum optimum," in the sense that market equilibrium on the basis of price relationships, with all its imperfections, would furnish us with a better set of solutions to the important economic problems than any alternative which is also deemed practicable. However, such an opinion should be formed, if at all, only at the end of this book, and not at the present point in the discussion.

*Making Economic Decisions in Wartime.* Our discussion of the making of economic decisions has dealt thus far with the operation of a capitalistic economy under ordinary peacetime conditions. Under the emergency conditions of wartime, the normal functioning of the price system may be almost completely suspended and economic decisions may be made on the basis of governmental planning and control. Theoretically, the expansion and contraction of various industries, the conversion and reconversion of productive

<sup>4</sup> *Ibid.*, pp. 188-191. Reprinted by permission of Farrar and Rinehart, Inc., New York.

facilities, and the allocation of land, labor, and capital among industries and businesses could be allowed to depend upon price relationships even in wartime. For example, the government might undertake to pay such high and profitable prices for airplanes that existing airplane factories would run at full capacity, automobile producers would voluntarily curtail or stop the production of automobiles and convert their facilities to the production of airplanes, and new firms would be induced to enter the field of airplane production. Similarly, the industries engaged in war production might attract the necessary workers by paying wages much higher than the workers could obtain in industries producing civilian goods, and so on.

In practice the government is likely in wartime to resort to direct control over production and over the extension and conversion of productive facilities. The reason is not that wartime problems are unusual in *nature*, but rather that they are unusual in *scope* and *urgency*. In peacetime, the conversion and extension of productive facilities occur gradually, and only a small number of industries may be seriously affected at any one time. In wartime, the conversion and extension of productive facilities are needed immediately, and most, if not all, industries are affected to some extent.

Moreover, if the banks are creating a considerable part of the funds necessary to finance the government's war expenditures (by buying government bonds and paying for them by creating demand deposits for the government), reliance on price relationships to induce the extension and conversion of productive facilities may be ineffective and costly. That is, if the government spends much more for war than it takes out of the current incomes of the people through taxes and direct sales of bonds, the willingness and ability of the government to pay high prices for airplanes may be offset to a considerable extent by the willingness and ability of private individuals to pay high prices for automobiles and other civilian goods. In such a situation, the extension and conversion of productive facilities may not go forward as desired, and the money cost of the war may be greatly increased as prices rise because of the competitive bidding of government and people for war goods and civilian goods, respectively. When agents of production are fully employed, competitive bidding for their services may result in serious inflation. Hence, in wartime, a government is likely to con-

trol prices directly and to regulate production through official boards or other agencies

Soon after the United States entered World War II, the task of speeding and guiding the output of necessary goods was assigned to the War Production Board, which was created by two Executive Orders issued by the President of the United States. The War Production Board was authorized (1) to exercise general direction over the war procurement and production program and (2) to determine the policies, plans, procedures, and methods of the several federal departments, establishments, and agencies with respect to war procurement and production, including purchasing, specifications, and construction, and including conversion, requisitioning, plant expansion, and the financing thereof, and to issue such directions with respect thereto as might be deemed necessary or appropriate. The Board established a number of regional offices, located in large cities from coast to coast, to facilitate the handling of local and regional problems.

The powers of the Board were, of course, very great. It could order industries producing civilian goods to curtail production or even stop operating altogether, and it could permit them to resume operations when needs for war production moderated to some extent. It could take almost any necessary steps to insure the adequate production of essential war goods. Conversion and extension of plant facilities could be undertaken only with the approval of the Board, and the Board controlled the allocation of vital materials and capital goods among firms and industries.

Under the so-called Controlled Materials Plan, prime contractors all over the country were required to assemble bills of materials needed, specifying kinds, quantities, and the times at which needed. These bills of materials were submitted to seven claimant agencies: Army, Navy, Maritime Commission, Aircraft Scheduling Unit, Board of Economic Warfare, Lend-Lease Administration, and Office of Civilian Supply. The claimant agencies combined the bills of materials sent in by their contractors and submitted them to the War Production Board, which matched total requirements of the claimant agencies with available supplies of materials, making allowances to the various agencies according to their importance. The claimant agencies followed their own preferences in distributing their allotments to the prime contractors, who in turn rationed the materials to sub-contractors. The allotments to contractors

amounted to "certified checks" for specific quantities of materials in specific periods of time. Finally, the War Production Board had to inform the producers of the materials what kinds and amounts of materials to furnish in order to meet the allocated demand in each period.

To these controls over production and the allocating of materials, add other controls over prices in general, the allocation of labor, the apportionment of finished goods among consumers, credit, foreign trade, and other matters and you have an erstwhile capitalistic economy which is difficult to distinguish from a planned and controlled economy. These other controls will be described briefly in appropriate later sections of the text.

### *Making Economic Decisions under Socialism*

*Socialism and the Price System* A socialistic economic system would face the same important economic decisions as a capitalistic economy, and it would in all probability, make use of money, credit, and prices. However, in the absence of private property in most productive wealth, freedom of enterprise, and competition, and with economic motivation emphasized less strongly than under capitalism, the operation of a socialistic economy probably would not depend upon price relationships to as great an extent as does that of a capitalistic system. Under socialism, according to a common interpretation, decisions as to the kinds and quantities of goods which would be produced would not depend on price relationships. Thus under socialism one of the major functions of the price system under capitalism would be eliminated. For all practical purposes society as a whole would be the only business enterpriser. Since society as a whole would both own and operate the land and capital of the system, interest and rent would not be paid and received as under capitalism. The planning authority or commission, which would be entrusted with the direction of economic activity under socialism, might charge itself with certain amounts of rent and interest for the land and capital used in various branches of production, but any such charges would be purely arbitrary, according to this interpretation, and would not result, of course, from competition between private owners of these agents and the persons desiring to use them in production. Wages of various kinds would constitute about the only money expense of production in the

ordinary sense under socialism. Wage differentials themselves would probably be adjusted so as to accomplish whatever results the planning commission thought were worth achieving, and would not result from competition between workers and private employers. Thus, the cost per unit of any economic good would be whatever the planning commission said it was.

Similarly, so it is said, the prices of finished products would not be determined by competition between buyers on the one hand and private sellers, organized under competitive conditions or those of monopoly or monopolistic competition, on the other. The prices of the various economic goods might well be set high or low by the planning commission according to whether it wanted to encourage or discourage the consumption of the various goods or whether the amounts available of the goods were large or small. Since both prices and costs would probably be arbitrarily determined by the same planning authority, the relationships which existed between such prices and costs would be virtually without significance and could not be depended upon for controlling the kinds and quantities of goods to be produced. The upshot of the whole matter is that, while prices and costs would be used as accounting devices under socialism and as convenient tools for making plans and supervising their execution, the basic decisions in the field of production would probably be made arbitrarily by the planning authority on the basis of social need for the products, or some other basis, and not on the basis of the prospective profitableness of producing the various kinds of goods.

Since society as a whole would own and operate land and capital under socialism, these agents of production would be distributed among the various industries and lines of production in such a way as to make possible the carrying out of the plans set up by the planning authority. Since the various industries and enterprises would probably never get a chance to bid various prices for the land and capital, the distribution of these agents among industries under such conditions would be in no way dependent upon the prices which these industries might be willing to pay for the agents. In other words, land and capital would be assigned arbitrarily to the various industries on the basis of the plans for production and the second function of the price system under capitalism—that of distributing the available quantities of agents of production among

industries—would be eliminated in so far as land and capital were concerned.

But the carrying out of general economic plans requires that labor, as well as land and capital, be distributed appropriately among industries. It is possible, of course, that workers, too, might be arbitrarily allocated to industries and occupations on a compulsory basis, but such a cavalier method of handling workers is rather improbable. Workers are human beings and the different workers have different abilities, find some occupations pleasant and others distasteful, prefer to live in different places, and so on. Their arbitrary assignment to certain tasks might well make for both inefficiency and dissatisfaction on the part of the workers, and this clumsy method would probably be held in reserve to be used only as a last resort. Again, something might be accomplished by moral suasion, slogans, and exhortations, or by offering various non-pecuniary incentives, such as leisure, vacations, special privileges, medals and insignia, and various public honors.

The distribution of labor among occupations could also be affected by raising and lowering the qualifications required of persons who desired to enter the various occupations. High requirements could be used to prevent the overcrowding of attractive occupations, and low requirements might keep less desirable occupations from suffering from a shortage of workers. However, the various sets of qualifications which would induce an appropriate quantitative distribution of workers among occupations might well set standards of competence which were too high in some occupations and too low in others from the point of view of social welfare, and it is questionable that low requirements would function effectively as a means of attracting workers to certain occupations. In all probability, then, the planning authority would provide for the payment of different rates of wages in different occupations and allow the workers a measure of freedom in distributing themselves among the various occupations on the basis of these differential wages. Low wages would be used to prevent too great a concentration of workers in the easy, safe, and pleasant occupations, while high wages would be used to insure the presence of at least a minimum number of workers in difficult, dangerous, and distasteful jobs.

The wage differentials used might not be nearly so large as under capitalism, and instead of being determined for the most part by

the competition of workers and employers as under capitalism, they would be set up, and varied at will, by the planning authority in order to obtain the desired distribution of workers among industries and occupations. In spite of these differences, it may be said that under socialism the distribution of workers among industries and occupations would depend upon price (wage) relationships to a considerable extent. However, something more than wage adjustments would be required to get workers out of declining industries. It would be necessary for the planning authority to discover new opportunities for the employment of the workers and to assist in caring for problems of transportation, retraining, and rehousing.

A socialistic system would also face the problem of rationing the limited quantities of finished goods among the consumers of the system. It is likely that this function would be performed to a great extent by means of price changes under socialism as under capitalism, although the necessary rises and falls in prices would result from orders given by the planning authority and not from the actions of individual buyers and sellers in the market. If, at a certain time, the available quantity of an economic good should be unusually limited, the planning authority would raise the price of the good so as to eliminate some buyers from the market; on the other hand, a low price would be used to induce increased purchases of some economic good which had been produced in unusually large amounts. As a matter of fact, this method of rationing might work better under socialism than under capitalism, since the planning authority probably would be uninhibited and would not hesitate to raise or lower individual prices by any amount necessary to bring market demand and market supply into equilibrium. However, under socialism, some rationing might well be done through quantities instead of through prices in order to make sure that all consumers would be able to obtain at least certain minimum amounts of scarce commodities.

The total amount of land available for production in a given economic system would be as fixed under socialism as under capitalism, and the total number of workers would probably be as little subject to wage influences under one system as under the other. However, a socialistic system would have to find some method of reaching a decision as to the extent to which the existing agents of production should be used to produce capital goods to assist in further production instead of being used to produce consumers'

goods for present enjoyment Under capitalism the processes of saving, investment, and capital formation are left to depend in large measure upon the reactions of individuals and firms to the changing relationship between the rate of interest and the prices of consumable goods, but under socialism this function of price relationships would probably be eliminated That is, the planning authority would decide to what extent capital goods should be produced, in order to achieve its other objectives, and it would accomplish its will in this matter by assigning existing land and capital to the production of capital goods rather than consumers' goods, and by paying high enough wages to attract workers to the industries producing capital goods The citizens of the economy would then "save" by going without consumers' goods, for each increase in the quantity of productive agents used to produce capital goods in a given period involves a corresponding decrease in the quantity of productive agents which are available to produce consumers' goods in that period, assuming full employment for the agents of production at the beginning of the period

The general impression furnished by this interpretation of socialism is that a socialistic economy would handle by means of economic planning most of the decisions which are supposed to be made under capitalism through the reactions of private individuals and firms to price relationships, and that these decisions would be made by the planning agency or authority in rather arbitrary fashion Ever so many economists hold that, while economic planning is undoubtedly necessary under socialism, the planning decisions must be made arbitrarily The reason for this opinion is easy to grasp An economy must have money as a common denominator for finished goods and agents of production, and the prices of all these things must be determined by the actions of large numbers of individual buyers and sellers in the market, if economic decisions based on rational calculation are to be possible The decisions of the economic planners in a socialistic economy must be arbitrary because they have no such market-determined prices of finished goods and agents of production to guide them

This does not mean that the planners cannot make economic decisions but it does mean that they can never be sure whether their decisions are well made They will know, of course, that a large amount of a good is ordinarily to be preferred to a small amount, but, having decided to produce a given quantity of a good

through the use of given quantities of the productive agents, they will never know whether that quantity of that good will give more satisfaction in relation to its cost than the quantity of some other good which could have been produced with the same quantities of the agents of production. Again, if the planners can order the production of an economic good by either of two methods, each of which requires a different combination of the agents of production, they can never be sure which method should be chosen. They may know and prefer the method which produces the greater amount of product, but they cannot know that this method was actually superior on the basis of cost.

The planners may decide to produce hundreds of thousands of tractors for agriculture, and the results of the decision may appear satisfactory since the tractors sell for "planned prices" which cover "planned costs," but the planners cannot be sure that the quantities of productive agents required to produce the tractors could not have been used to produce low-cost housing for the citizens with a greater sum total of satisfactions resulting. Again, if a certain quantity of an agricultural product can be produced by intensive methods but a greater quantity can be produced by extensive methods which require greater quantities of land, the planners may choose the latter method but they cannot be sure that their decision would have been appropriate if the land and the agricultural product had been priced in a competitive market.

*Rational Allocation of Productive Resources under Socialism.* However, there are some economists who do not accept this common opinion to the effect that all the important economic decisions would have to be made arbitrarily by the economic planners under socialism. They see a possibility for the rational allocation of productive resources even under socialism, although the process by which this result might be achieved would be highly complicated. According to Pigou, for example, we might start by defining rational allocation to mean such a distribution of productive resources that the marginal private cost of each good would equal average cost, and the average cost of each good would equal demand price. We assume at first that the productive agents last forever and that no new ones can be made, that the processes of production and distribution are instantaneous so that no working capital is necessary, that all workers are alike and receive equal incomes, and that there

are no other productive resources, and we ignore the fact that some goods are produced jointly and that others require successive stages of production at the hands of several industries. Labor is originally distributed roughly and arbitrarily among industries, and then its distribution is adjusted so that there is no shortage or surplus of any good and so that the amount paid out in wages in each industry is equal to the total sum received from the sale of the product of that industry.

The next step is to bring in the other agents of production and, since there are no market-determined prices for the use of these agents, arbitrary "accounting" prices for their use must be established by the planning agency. These accounting prices are deemed correct when, on the basis of these prices, all the industries (with each operating so as to minimize average accounting costs of production) precisely absorb all the workers and productive instruments. The productive agents are distributed roughly among industries at first, and then each industry is charged with the task of varying output so that (1) there will be no shortage or surplus of any economic good, (2) each industry will receive a total income from sales which will equal total costs on the basis of the accounting prices for the productive agents, (3) the average accounting cost of each industry's product will be a minimum, and (4) the workers as a whole will get just enough income to buy all the products available for their use. After all adjustments have been made, it will be found that accounting prices for some agents have been set too high and those for others too low, and that some units of some agents will be unused while industries would gladly use more than the total quantity of other agents. The accounting prices of the agents must then be adjusted, and this calls for a further set of adjustments all the way down the line.

We must also account for the different kinds of labor. If we assume that all workers are alike except for training and that the cost and time of training are the same for all occupations, the planning authority must decide how many workers should be trained for each occupation, select the workers, train them, and fit them into the scheme we have been discussing. Further adjustments would be required to take account of the varying abilities of workers, which cannot be produced by training, the joint production of some goods, the several stages of production required for

others, and any international influences which might affect the situation. Eventually the complete rational allocation of productive resources might be achieved<sup>8</sup>.

Even so, the planning authority would have to realize that certain instruments of production do not last forever, that additional quantities can be produced, and that working capital is necessary. While the planners will have set up accounting rates of interest for the purpose of allocating available capital funds among industries, such accounting rates of interest will not be useful in deciding what part of the economy's resources should be devoted to the production of capital goods and consumers' goods, respectively. This decision must be made arbitrarily, but there is some question as to whether or not this would be a great disadvantage. A socialistic economy would be no worse off than a capitalistic economy in deciding what part of total resources should be devoted to investments in armaments, roads, education, and health, and might actually reach superior decisions on the latter two types of projects.<sup>9</sup> The claim that a socialistic economy would be too far-sighted and inclined to overweight the future may be countered by the claim that a capitalistic economy traditionally overweights the present. Thus, while the type of decision under discussion would be made arbitrarily, there is no reason to assume that the decisions actually reached would be worse than those of a capitalistic economy.

We shall now examine briefly another approach to the problem of rational allocation of productive resources under socialism. According to Dickinson, such a rational allocation will be considered as achieved only if (1) all productive resources are fully utilized, (2) the prices of all goods are equal to cost, (3) among alternative methods of production, that one is always chosen which turns out the product at least cost, and (4) each production good with alternative uses is so distributed that its marginal net product in each use is equal to its price. In order to obtain these results, it must be possible to compare the satisfaction to be derived from extra goods with their cost and to compare the cost of using alternative methods of producing a given good. Since the agents of production do not have market-determined prices, arbitrary or accounting prices must be set up for all agents, or for all agents except labor.

<sup>8</sup> This discussion is based on A. C. Pigou, *Socialism versus Capitalism*. London: Macmillan and Company, Ltd., 1937, Chapter 7.

Once costs have been set up, it is possible to choose between goods and between different methods of production, and the principle of substitution can function. The original prices of goods and agents of production, and the distribution of the agents among industries, will be very arbitrary, but eventually both the prices and the distribution can be adjusted so that they conform to the principles of scarcity and substitution. If some agents of production are given accounting prices which are too high, some units of these agents will be unemployed. If the prices of other agents are set too low in relation to their scarcity, industries will try to obtain larger quantities of these agents than are available. The initial stage of rational allocation is reached by adjusting the prices of the agents until all are just fully used. Then industries will have an incentive to substitute, where possible, those agents whose prices have fallen for those whose prices have risen. This may require further changes in factor prices, and so on, but with each set of changes smaller in magnitude than the preceding set.

The next stage is found in applying the principle of cost to both finished and intermediate goods. It will be discovered that, after the preceding adjustments, some of the goods are priced below cost and others above cost. As the prices of some goods are raised and those of others are lowered, additional factors of production will be drawn into making the former goods and some units of productive agents will be forced out of the making of the latter goods. This redistribution of the productive agents will call for further readjustments all along the line, but this is the last stage in the attainment of rational allocation if the available quantities of the productive agents are taken to be fixed. However, the recognition that different kinds of capital goods, at least, are variable in quantity over any extended period of time will lead the planning authority to make decisions as to the disposition of the economy's resources between providing for the present through the production of consumers' goods and providing for the future through the creation of capital goods. These particular decisions must be made arbitrarily, but, once they are made and additional quantities of capital goods are available, they will lead to further changes in the prices of productive agents, to further redistribution of the productive agents, and to the repricing of various finished commodities and services. These changes mark the fourth and final stage of

the process of rational allocation of productive resources under socialism

When all adjustments have been made, the result is supposed to be an equilibrium situation in which full account is taken of consumers' preferences as expressed in the prices of final products, producers' preferences as expressed by the supply of labor available at different rates of wages, and the technical conditions of production. The process of attaining rational allocation is divided into four stages only for the purpose of analysis, and not because the different types of adjustment would actually be made one after another. Actually all the phases of adjustment would be carried on at the same time. The whole problem of attaining rational allocation of productive resources under socialism is, according to Dickinson, comparable in complexity to that of solving two or three thousand simultaneous equations with the data themselves constantly changing.<sup>6</sup>

Although the attainment of rational allocation under socialism is quite possible as a strictly theoretical proposition, the difficulty of attaining it in practice would be so great that it is easy for us to imagine the economic planners throwing up their hands in disgust over the whole matter and deciding to determine by themselves as best they can what kinds and quantities of goods the people want or should have, how the agents of production should be distributed in order to produce these goods, how the goods should be distributed among the consumers, and how the resources of the economy should be divided between providing for the present and providing for the future. In order to have any idea of what they were doing, however, the planners would have to set arbitrary prices for the use of land and capital. When goods must be produced on soils of varying fertility or from natural resources of varying quality, expanding production will lead to increasing cost per unit of product if productive methods remain unchanged and if the best grades of soil or other resources have been brought into use first. If the resulting products were valued according to their average cost per unit, the production of such goods would probably be overextended because their cost would be, in a sense, underestimated. The use

<sup>6</sup> For a more complete discussion of this approach to rational allocation, see H. D. Dickinson, *Economics of Socialism* Oxford Clarendon Press, 1939, Chapter 3.

of marginal costs, or the costs of adding units of such products, would be better as a means of deciding how far to carry production, but their use would involve taking economic rents into consideration, even though rates of rent would have to be set up quite arbitrarily.

Again, arbitrary interest rates would be necessary in deciding how to distribute available capital goods, or funds for investment in capital goods, among the various industries. Moreover, while arbitrary interest rates would furnish no basis for rational calculation in connection with providing for the present and providing for the future, an interest concept, at least, would be necessary in making decisions of this kind. Attempts to increase production often involve the use of more and more roundabout methods of production, or methods which will produce a greater physical product but only at a relatively more remote point in time. The interest concept is necessary in deciding how great the future increase in physical production needs to be, how remote the increase in production may reasonably be, and what part of the economy's resources may well be devoted to such remote objectives. If no interest concept were used, the planners would overexpand the production of goods whose production required productive methods more time-consuming than the average, and they might consider it equally desirable to produce either of two goods which required the same amounts of the basic productive agents, land and labor, even though one good required a productive process which was much more time-consuming than that necessary for the other.

The results of using arbitrary rates of rent and interest probably would not be too unsatisfactory if the economic planners were able to form, and were willing to act upon, reasonably accurate estimates as to the kinds and quantities of economic goods which the citizens of the economy wanted. However, such estimates might be rather difficult to obtain. The planners could make use of the opinions of experts or of advisory bodies of consumers in trying to determine the needs and desires of the citizens, but it is difficult to be a real expert in this field and the opinions of experts or advisory bodies as to what people wanted, or should have, might not coincide at all well with the views of the citizens. The planners might make use of questionnaires and polls but, quite apart from the question of the reliability of such devices in getting information on the relative strength of desires for various economic goods, it

would probably not be feasible to use such techniques in connection with all the thousand and one goods which a modern economy must produce

The planners could rely in part on knowledge of what people had consumed on the average in the past under capitalism and could make adjustments on the basis of what people in good, though not rich, circumstances had consumed in the same situation. Such information would have to be recent in order to be of much value and, if an attempt were made to get around this obstacle by using an existing capitalistic system as a basis for estimation, further difficulties would be encountered. It would be hard to decide what other economy, if any, could be regarded as strictly comparable to the socialistic system, the method obviously could not be used in a socialistic world in which no capitalistic system remained, and many socialists would probably regard it as shameful in any case if their brave new world of the future had to depend upon an existing and presumably decadent capitalistic system for information on such a vital matter.

Finally, the planners could get some information as to the success of their production policies in satisfying human needs and desires by observing the alacrity or reluctance with which consumers took available quantities of economic goods off the market at planned prices. However, it is most difficult to get any accurate information concerning the demand of consumers for a particular good in a market situation in which the quantities and prices of other goods are rigidly controlled. If the planners observed that consumers purchased and ate a kilogram (2 2 pounds) of bread per day on the average at planned prices, it would be easy to decide that the citizens were bears for bread unless one reflected that this reaction might be due in part to the fact that butter was practically unobtainable and priced very high. That is, in a perfectly free market the consumers might well have preferred more spread and less bread.

All this discussion, moreover, seems to presuppose that the planners struggle manfully to make their economic decisions coincide with the needs and desires of the citizens and that, if the planners do not make "good" plans, they can be removed from office and a new group of planners substituted for them. If the planners do not care what the people want, or decide that they know what the people should have and try to educate the people to want those

things, or more especially if the planners' first plan is an ironclad scheme for keeping themselves in office as planners regardless of the success or lack of success with which they adapt production to the needs and desires of the citizens, the results may be most unfortunate. The success of economic planning, from the point of view of the citizens, clearly depends to a considerable extent upon the nature of the government which the socialistic system has. The upshot of the whole matter is that we cannot be sure, merely by substituting economic planning for the price system, that the economy will do a perfect job, or even a better job than the capitalistic system does, in adjusting production to the basic needs and desires of the citizens.

**Conclusions** We see, then, that the operation of a socialistic economy depends on economic planning, that is, on "the making of major economic decisions—what and how much is to be produced, how, when, and where it is to be produced, and to whom it is to be allocated—by the conscious decision of a determinate authority, on the basis of a comprehensive survey of the economic system as a whole".<sup>7</sup> The socialistic economy depends on economic planning because it must. Although it makes use of a system of money and prices, the prices of finished commodities and services and those of agents of production are not determined by the competition of numerous buyers and sellers in the market and hence are not reliable guides for the making of important economic decisions. A socialistic economy not only needs economic planning but also has the ability to make comprehensive economic plans and to see to it that these plans are carried out as thoroughly as possible. This is because the productive wealth of the system, consisting of land and capital, is owned by society as a whole, and society as a whole, through the government, is the only business enterpriser of any importance and operates practically all lines of economic activity.

We see also why it is that a capitalistic economy cannot operate on the basis of economic planning. Of course, the government of a capitalistic economy can engage in partial economic planning by intervening in various phases of economic activity, but attempts, for example, to control the development of industry by means of a protective tariff or to handle an unemployment problem by giving

<sup>7</sup> From *Economics of Socialism* by H. D. Dickinson (Clarendon Press, Oxford) p. 14 by permission of the publishers.

governmental aid to declining industries may well do more harm than good, and they lead to all manner of attempts by pressure or interest groups to bring undue influence to bear on the government. If the government actually owns and operates some industries under capitalism, it assumes at least part of the role of a private employer and must usually compete with private enterprisers for capital or other productive agents. Full-fledged and comprehensive economic plans for the economy as a whole could be drawn up by the government of a capitalistic system, but under capitalism it lacks the power to see to it that these plans are carried out. If the plans happened to coincide with the interests of private enterprisers and private owners of land and capital, the plans might be carried out but the time and effort given to the making of the plans would have been largely wasted, since private enterprisers and owners are expected to act in their own interests in any case under capitalism. If the plans did not coincide with the interests of private enterprisers and private owners of land and capital, these people, secure in their freedom of enterprise and in their ownership and control of productive wealth, would simply refuse to carry out the plans, and the time and effort given to their construction would again have been wasted. It is conceivable, of course, that the government might take over the *control* of land and capital while leaving their *ownership* in private hands. Such a course of action might make economic planning work, but a system in which the owners of land and capital did not control and operate these agents would not be capitalistic except perhaps in name.

The same lack of market-determined prices for finished commodities and productive agents which makes it necessary for a socialistic economy to engage in economic planning also makes it necessary, according to most economists, for all important economic decisions to be made more or less arbitrarily by the economic planners under socialism. It is possible, as we have seen, to devise processes in theory by means of which a socialistic economy could obtain most of the effects of the capitalistic price system without actually having that system, but it is not likely that a socialistic economy could achieve a strictly rational allocation of productive resources among industries in practice. And, in any case, many important economic decisions would have to be made rather arbitrarily under socialism. These decisions would include (1) the allocation of resources as between providing for the present through

the production of consumers' goods and providing for the future through the production of capital goods, (2) the making of choices as between working to obtain additional goods and having leisure time for the enjoyment of present income or for other purposes, and (3) the allocation of resources between individual consumption and communal consumption or consumption in common. However, these decisions are also made rather arbitrarily under capitalism. For example, the allocation of resources between present and future consumption depends not merely on the actions of individual savers on the basis of prices, interest rates, and time preference, but also on corporate savings, monetary policy, the way in which the banking system is operated, forced savings, the balance of international payments, and other factors.

✓ Just how well a socialistic economy could operate on the basis of economic planning to adjust the kinds and quantities of goods produced to the real wants of consumers, to allocate productive resources among industries, to produce all goods as efficiently as possible, and to get goods distributed equitably and efficiently among consumers, cannot be determined on an *a priori* basis. However, according to most socialists, a socialistic economy could hardly operate less satisfactorily than a capitalistic economy. While a socialistic economy would not work perfectly, says Strachey, it "could not do anything so insane or so horrible as to produce a plethora of yachts and beauty parlors while millions of men and women lack for food and shelter, it could not succeed, as does our present system, in simultaneously torturing the town workers with a lack of bread and ruining the farmers by a glut of wheat".<sup>8</sup>

#### QUESTIONS

- 1 "Rises and falls in the prices of finished economic goods and of the agents of production necessary to produce them control the kinds and quantities of economic goods which will be produced under capitalism." Explain.
- 2 How are existing supplies of productive agents allocated or distributed among enterprises and industries under capitalism? Explain.
- 3 A few decades ago there was no automobile industry in the United States. Now it employs many thousands of workers. How does such a developing industry obtain its labor force under capitalism? Explain.

<sup>8</sup> John Strachey, *How Socialism Works*, pp. 44-45. Reprinted by permission of the author.

4. Limited supplies of finished economic goods may be rationed among consumers either through price changes or by limiting the quantities which individual buyers may purchase in given periods of time. Compare these two methods of rationing as to efficiency and effects on consumers
5. How effective are price changes in controlling the total amounts of productive agents through time? Explain
6. "If our capitalistic system operated perfectly on the basis of price relationships, the result would be not only economic equilibrium but economic optimum" Show whether you agree
7. What are some of the obstacles to the attainment of full economic equilibrium on the basis of price relationships under capitalism? Explain
8. What is the significance of great inequality in the distribution of income in connection with the question of whether economic equilibrium on the basis of price relationships would also be an economic optimum? Explain
9. "The price mechanism under capitalism is defective in that it does not permit the expression of certain negative preferences of individuals nor of certain complex positive wants" Explain
10. "Ideal freedom of consumers' choice would be somewhat more comprehensive and less detailed than that which consumers actually have under the operation of the capitalistic price mechanism" Show whether you agree
11. How and why is the capitalistic method of making economic decisions likely to be modified in wartime? Explain
12. "Under socialism, some functions which prices perform under capitalism would be retained, while others would be modified or eliminated" Explain
13. "Under socialism, land and capital would be distributed among industries in one way while workers would be distributed in quite a different way" Why?
14. Compare the process of saving and capital formation under socialism with that which exists under capitalism
15. "A socialistic economy must also be a planned economy" Explain
16. What is meant by saying that important economic decisions must be made "arbitrarily" by the economic planners under socialism?
17. Discuss the prospect of achieving a rational allocation of productive resources under socialism
18. "The difficulty of discovering and measuring the needs and desires of the citizens is perhaps the chief obstacle to the rational allocation of productive resources under socialism" Do you agree? Explain
19. "If economic planning is as effective as the socialists contend, we should adopt it as the method of operating our capitalistic system" Show whether you agree

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## CHAPTER 6

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### **MAKING ECONOMIC DECISIONS**

(Continued)

#### *Making Economic Decisions\* under Communism*

If communism were carried to its logical conclusion, anarchistic communism, in which there would presumably be no government and no price system or economic planning, it is difficult to see how the important economic decisions would be made. Each individual would be supposed to select that occupation in which he would be most useful to society as a whole, function to the best of his ability, and consume on the basis of needs, but it is impossible to determine how these activities of individuals would be put together and coordinated into an appropriate whole. The problem of making economic decisions under communism would be thorny enough in the absence of any system of prices and costs, even though government and economic planning existed. All enterprises would apparently contribute to and draw out of a common stock pile according to plan, and finished goods and agents of production would circulate and be distributed without sales or purchases. Economic planners would study data on needs, take into account the available agents of production, and distribute them as best they could. However, it is very difficult to determine needs on any *a priori* basis. They can be estimated only roughly for such items as food, clothing, and shelter, and the problem is still more complex for other categories of goods.

Of course, a communistic system might try to overcome its deficiencies by estimating values in terms of labor time. This would probably involve the development of a labor day of given productivity and the adaptation of this concept to all types of industries. However, there would be no way to measure differences between

skilled and unskilled labor except by some type of arbitrary coefficient, and even that device would be useless where differences between workers depended upon hereditary qualities which could not be reproduced by training. Since most industries make use of machines and materials which are obtained from other industries, it would seem necessary to have labor values set up for the entire system before any industry could use them. Within industries, it would be readily possible to compare value with cost only when all enterprises had about the same kind of internal structure, that is, when they used about the same kinds and qualities of labor. This would not usually be true, and the case would be even more hopeless when the enterprises operated under varying natural conditions and made use of capital in different degrees. If different enterprises used lands of different quality or located varying distances from the market, the labor-cost concept would not be a reliable guide to economic organization. Again, while it is true that production which used much capital would have a lower total labor cost than that which used little capital, it would be possible to decide that the more roundabout method should always be used only if capital were unlimited, which it never is in practice. The economy might decide to abandon an industry with low labor costs and start up an industry with higher labor costs if it could be determined that the product of the latter industry were more needed or desired than that of the former industry. In other words, social needs or demands are important in determining values as between industries, but it is difficult to take these matters into account in the absence of money and prices.

### *Making Economic Decisions in Soviet Russia*

As we have said, the economic system of Soviet Russia seems to be more nearly socialistic than anything else, and it operates on the basis of full-blown economic planning. However, the Russian economic system did not change from capitalism to a planned economy overnight. For about nine months after the revolution, or until the middle of the summer of 1918, an attempt was made to operate on the basis of what might be called state capitalism. That is, the party in control of the government sought to nationalize the banks and secure control over the capitalististic economy of Russia without dis-

rupting or destroying its internal organization This system failed to operate successfully and a new expedient had to be tried

*The Period of "War Communism"* From midsummer of 1918 until March, 1921, the Russian economy operated under a system commonly known as War Communism The system was described as a temporary expedient (so that it could be replaced quickly in the event of failure), but the steps which were taken were intended to be permanent, if successful The Supreme Economic Council was supposed to manage industry, and an organization known as the Labor and Defense Council was to direct the economic system as a whole, make economic plans, submit them to the All-Russian Executive Committee for approval, direct the work of governmental departments in accordance with the plans, and supervise the carrying out of the plans Market transactions were suspended, the use of money was discontinued, and wages were received in terms of commodities, with many services provided freely by the government All goods were to be turned over to the central authorities and to be distributed by them From all accounts, this impromptu system of communism worked most miserably in the face of great resistance Russian agriculture was virtually ruined by civil war, the agrarian revolution, and attempts by the government to requisition or confiscate surplus products Industrial production was also at low ebb, falling to 20.4 per cent of the 1913 level by 1920,<sup>1</sup> for the workers lacked incentives and never knew what kinds and amounts of goods they might receive for their services There was a great famine in 1921 and 1922, and the leaders of the government were greatly concerned over the increasing hostility of peasants and industrial workers

*The New Economic Policy* Accordingly, the New Economic Policy was introduced in 1921 in an effort to increase production sharply and overcome the political crisis The government kept its control over such commanding heights of economic activity as large scale industry, transportation, the banking system, and foreign trade, but many other sectors were reopened for private enterprisers and business men Markets were restored, and money and prices were again used The private and socialized sectors of the economy were supposed to cooperate and were connected with each other in the market Under this system, economic activity revived almost at once,

<sup>1</sup> Alexander Baykov, *The Development of the Soviet Economic System* New York The Macmillan Company, 1947, p. 8

private enterprises showed a great deal of life, domestic trade flourished, and industrial production in general regained its 1913 level by 1926-27, though there was considerable variation in the degree of recovery experienced from one branch of industry to another.<sup>2</sup> In any case, the private enterprises had no legal status or protection against the government and, before very long, their activities were limited or their capital was taken over by the government.

The State Planning Commission, which had existed since 1921, began to put out Economic Control Figures for the Russian economy starting with the period from October, 1925, to September, 1926. The various state departments of economic activity were supposed to give consideration to these control figures in drawing up their own plans, and the figures were supposed to be useful in predicting the development of production and trade, in maintaining an equilibrium of demand and supply on the market, and in preserving the free market connection between the private and socialized sectors of the economy. The control figures appeared annually and became more and more binding on the operation of the economy. Finally, on October 1, 1928, the Russian system began to operate on the basis of its First Five-Year Plan, which was scheduled to last through September, 1933, but was actually declared completed at the end of 1932. The Second Five-Year Plan was in effect from 1933 to 1937, and the Third Five-Year Plan (1938-1942) was interrupted by the German invasion in 1941. After a lapse of several years during World War II, the Fourth Five-Year Plan was undertaken in 1946 and was to last through 1950.

*Conditions and Objectives of Economic Planning* In Soviet Russia, the society as a whole, operating through the government, owns all the land and by far the greater part of the capital of the system, most fields of activity are dominated by governmental enterprises, and a strong, unified leadership is present. The essential conditions of economic planning are therefore at hand, and the economy, since its money prices and costs are not market-determined, needs to operate on the basis of economic planning. Russian economic planning, however, has not been contented with merely making the system operate. It has also aimed at such objectives as increasing the national wealth, the rapid industrialization of the economy, the collectivization of agriculture, the reduction of costs,

<sup>2</sup> *Ibid.*, p. 121

of production and the increasing of labor productivity, a steady increase in both the material and cultural standards of the citizens, and the strengthening of the independence of the country and its ability for self-defense.

*The State Planning Commission* The chief planning agency in the Soviet Russian system is the State Planning Commission, or Gosplan, which is, as we have seen, appointed by and responsible to the Council of Ministers, the highest executive agency of the Russian Government. As reorganized just before World War II, it consists of a President, a Board of 11 members, and a Council of 70 members. The members are selected from among the leading planning workers, scientific workers, and specialists of the country. The Commission is organized into four departments (general economic plan, capital construction, finance, and regional distribution of production) and 26 sections each of which deals with some special branch of economic activity. The Commission's duties include (1) the working out of economic plans of all kinds and their presentation for review by the Council of Ministers, (2) presenting the Council of Ministers with conclusions concerning the plans which are worked out by various subsidiary planning organizations, (3) reviewing the execution of the plans, (4) the study of various individual economic problems, (5) the appointment of expert commissions to handle specific economic questions, (6) the working out of questions of planning methodology, and (7) directing the work of socialist accounting.<sup>3</sup>

The State Planning Commission receives a great deal of help with its work of economic planning. In fact, one of the most difficult phases of planning—the choosing of goals or objectives—is not handled by the Commission. That is, the leaders of the Communist Party give the Commission general directives as to what should be accomplished in the period covered by a given plan and the Commission is supposed to work out the specific ways and means of accomplishing these general goals. The Commission is given a great mass of statistical data with which to work. It has an estimate of population, corrected for those who are too old or young to take part in productive activities, those who are disabled, and those who are engaged in study and research, administration, national defense, and housework, and all enterprises and agencies

<sup>3</sup> *Russian Economic Notes*, Number 363, pp. 8-11. Washington Department of Commerce, Bureau of Foreign and Domestic Commerce.

in the economy furnish complete information as to what they have accomplished in the past, their present status, and what they think they can do in the future.

The State Planning Commission has the help of a large staff of workers and is also able to rely upon the services of the Central Statistical Administration, the Central Administration of National Accounting, the Molotov All-Union Academy of Planning, and the Academy of Sciences with its scores of research institutes. There are also many other subsidiary planning organizations which are supposed to be of assistance to the State Planning Commission. Each Ministry or governmental department has its own planning agency, and the same thing is true of most of the economic units or agencies in the system, such as administrations, trusts, factories, stores, collective farms, state farms, transportation agencies, and so on. These planning agencies are known as functional subsidiaries. On the other hand, planning agencies, known as regional subsidiaries, are maintained by the various republics, provinces, regions, and even many communities. In both the functional and regional organizations, each planning agency is responsible to the next higher agency and so on up to the State Planning Commission, which has the task of coordinating the activities of the functional and regional agencies.

The Five-Year Plans have been so well publicized that many people think that the Russian economic plans are made only at five-year intervals. Actually this is anything but the case, for economic planning is a completely continuous process and there are annual plans within each Five-Year Plan and quarterly plans within each annual plan. There are even monthly and five- or ten-day plans for plants or groups of plants in specific branches of industry. Each Five-Year Plan is a definite plan only for one year in advance, and a tentative and preliminary survey for the four following years while some very general plans are laid down for periods of ten or fifteen years in advance. The Five-Year Plans are subject to perpetual revision as they are carried out and, as a matter of fact, there seems to be no real reason why the planning process should be broken up into five-year intervals except to give an occasional fresh stimulus to the people and to maintain their interest in and enthusiasm for planning.

*The Planning Method.* However, we may use the construction of a Five-Year Plan as an illustration of the planning method which is

used When a new Five-Year Plan is to be constructed, the State Planning Commission, with all the resources at its disposal, first sets up a tentative but comprehensive plan covering virtually all phases of economic and non-economic activity for the period in question When the plan has been formed, it is broken up into sections and each section is sent to the appropriate Ministry or department for consideration The plan is then divided up still further, and each administration, trust, factory, collective farm, state farm, transportation agency, or other economic unit, and each republic, provincial, regional, and community planning agency, receives the part of the plan which pertains to its operation during the next five years A factory, for example, would receive information as to the kinds, quantities, and qualities of goods which it was expected to produce, quantities and kinds of labor, power, materials, capital goods, and other things which would be supplied to it, estimates of the productivity which the workers should achieve, and estimates of the workers' incomes and living standards

The various subsidiary planning agencies of a functional and regional character submit their various parts of the plan to careful consideration and discussion In the lowest economic units of the system, in the factories and on the farms, even the workers are supposed to have a chance to discuss the plans and make suggestions concerning them The result of all this consideration and discussion is supposed to be a great volume of suggestions, criticisms, and counter-plans for the guidance of the State Planning Commission As the period allotted for the consideration of the plan approaches its close, the suggestions, criticisms, and counter-plans are assembled from factories, farms, and other basic economic units up through trusts and administrations to the Ministries, and from community planning-agencies up through regional, provincial, and republic planning-agencies to the Ministries The planning agencies of the Ministries organize this material and turn it over to the State Planning Commission for consideration

The Commission reconsiders its original plan in the light of the great mass of suggestions, criticisms, and counter-plans which it has received and eventually works out the final plan There is some disagreement among writers as to the importance of the suggestions, criticisms, and counter-plans received from below and their influence, if any, on the final plan drafted by the Commission Some consider these materials very important and helpful and suggest

that the final estimates as to quantities and qualities of goods to be produced, as to labor productivity, and as to cost of production are altered materially as a result of the suggestions and criticisms received by the Commission from the functional and regional subsidiaries. Others claim that the Commission goes ahead to formulate the final plan with very little reliance on the suggestions and criticisms received from below, that these materials are of little value since they always call for results more favorable than those proposed originally by the Commission and are never genuinely critical of the tentative plan, that an "improper attitude" toward planning on the part of the individuals who make up the subsidiary planning agencies is punishable, and that the Commission calls for suggestions, criticisms, and counter-plans only to keep the people aware of the planned nature of their economy and the problems of economic planning and to stimulate interest and enthusiasm in connection with planning.

If the Commission gives any great amount of attention to the suggestions, criticisms, and counter-plans, it is obvious that it has an enormous task on its hands. Consider, for example, just one item—the distribution of the fund suggested by the plan for developmental purposes in the coming period.

How shall this be allocated? The Labor Unions press for a big increase in the insurance funds as well as in wages. Each Commissariat likewise wants a good slice of it. Each republic puts forward its claim for the development of new railways and mines. Every city and town is clamoring for more schools, buses, sewers, clinics. From these rival claimants and the welter of conflicting interests, rigid selections must be made. Which are absolutely essential and imperative now? Which can be postponed for a year, five years, or a decade? Each claim is considered on its own merits and in the light of its contribution to the weal of the nation as a whole. In the hotly contested debates, out of the endless weighing of pros and cons, the balancing of economic, political, and military considerations, finally emerges the plan.<sup>4</sup>

If we apply this general analysis to the various sections of the plan, we have some idea of the task which confronts the Commission.

When the final plan has been made, it is submitted by the Commission for approval at the hands of the All-Union Congress of the Communist Party or the Supreme Soviet of the U.S.S.R., or both. This approval is, of course, a mere formality. With the State Plan-

<sup>4</sup>A. R. Williams, *The Soviets*. New York: Harcourt, Brace and Company, Inc., 1937, p. 187. Reprinted by permission of the publishers.

ning Commission and the subsidiary planning agencies completely controlled by the Communist Party, it is unthinkable that the final plan submitted could be one which would not meet with the approval of the Communist Party, or of the Supreme Soviet which is itself entirely dominated by the Communist Party. After the final plan has been approved, it is divided and subdivided and the parts are sent out to the Ministries and to the various functional and regional planning agencies. Thus, in the end, each economic and geographical or other agency has before it detailed and specific plans covering its operation and functioning during the next year and somewhat more tentative plans for its work over the entire five-year period.

The final plan is long and immensely complicated. The First Five-Year Plan filled three volumes which totaled some 1600 pages and the second plan was stated in two volumes containing 1300 pages. The plans contain sections covering the developments which are to occur in the fields of industry (machine building, electric-power stations, timber, chemistry, fuel, mining, foods, consumers' goods, and many other phases), agriculture, transportation, communications, and construction. Special sections are devoted to such questions as labor productivity, wages, costs of production, standards of living, quality of goods, distribution of goods, and per capita consumption. Sources of funds, money in circulation, and the volume of credit are provided for, and projects are outlined in connection with education, public health, social insurance, housing, and the reduction of illiteracy. For these and many other items, specific goals are established and methods of reaching these objectives are specified.

*Problems of Planning.* In so far as we can determine, the economic planners of Soviet Russia make no attempt to secure the results of a capitalistic price system without actually having such a system. That is, they apparently do not grapple with the problem of obtaining what has been called a rational allocation of productive resources among industries. It is the duty of the State Planning Commission, assisted by all the agencies and materials which have been mentioned, to make the final decisions as to the kinds and quantities of economic goods which the citizens of the economy want or should be allowed to have, the allocation of available resources among industries and fields of economic activity, the balance which should be achieved between present consumption and capital formation,

and, to a great extent, the way in which the products of economic activity should be distributed among the people. In the absence of market-determined prices and costs, and without any attempt to achieve rational allocation by artificial means, these decisions must be made rather arbitrarily by the State Planning Commission (to the extent that they are not made for the Commission by the leaders of the Communist Party)

The citizens of the system as consumers have no choice as to the directions which socialistic investment will take or as to the kinds and quantities of economic goods which will be produced, and the planners have no direct guidance as to the relative magnitudes of the various desires and demands of the consumers. The Commission has some idea of the relative intensities of consumer demands on the basis of the planned prices which are charged, but the very fact that these prices are planned and fixed impairs the value of this knowledge as a basis for making economic decisions. The fact that the turnover tax, as applied to the sale of various economic goods, yields widely varying amounts of revenue from one type of good to another suggests that the relation of planned selling price to planned cost of production is also quite different from one economic good to another. This in turn indicates that the industrial output of various economic goods is quite imperfectly adapted to the underlying demands of consumers. Moreover, even if the Planning Commission had extensive knowledge of the effective demands of consumers, as indicated by their willingness to pay money prices, this would not mean that the Commission really understood the basic subjective desires of the people if different classes of people were allowed to receive widely varying amounts of money income.

The Commission may provide for the production of a certain quantity of an economic good in a given year, and the entire quantity may be readily taken off the market at a planned price which covers planned costs, but the Commission can never be sure that the same quantity of productive resources could not have been devoted to the production of a quantity of some other good with a greater total satisfaction resulting. In such a case, the industry which actually uses the resources might be seen as operating at a loss, when carried on to its present extent, if the final products and agents of production had market-determined prices. Again, in choosing between different methods of producing a given good, when the methods require different combinations of the productive agents

and produce different amounts of the product, the Commission may be able to justify its decision on the basis of planned prices and costs, but it can never be certain that its decision would have been justified on the basis of market-determined prices and costs.

It is too much, then, to expect that the decisions of the State Planning Commission will be perfectly adapted either to the basic desires of the Russian consumer or to the relative scarcities of the productive resources. Moreover, once the plans have been made, for better or for worse, there is anything but certainty that the plans can be perfectly fulfilled. As we have seen, the essential conditions for economic planning are present in Soviet Russia, but there are many things, which are beyond the control of the economic planners, which may have an important effect on the possibility of carrying the plans through to fulfillment. For one thing, natural phenomena are beyond the control of economic planning. Floods, droughts, and other natural events occur in rather unpredictable fashion and may cause the outputs of certain important crops to deviate widely from the results called for by the economic plans. Since such agricultural products are the basic raw materials for a variety of other industries, short crops (or unexpectedly large ones) may have important repercussions in other fields of economic endeavor. It will be impossible to maintain planned outputs of tires, clothing, and textile materials of other kinds if the cotton crop is a failure, and the output of flour is dependent on the wheat crop in the last analysis even if considerable stocks of wheat are held. On the whole, it would be much easier to care for the situations created by bumper crops than those which result from small crops, but large crops would nevertheless be expected to cause industrial outputs to deviate from the planned figures.

Technological change is another factor which is at least partly beyond the control of the planners. New tools and machines are invented, better managerial practices are developed, and improved methods of operation are discovered by workers. All these things are capable of upsetting planned outputs. Of course, a staunch supporter of capitalism might argue that a planned economy would not have to worry about these things since, in the absence of large pecuniary incentives, people would not develop new machines and methods of production. However, these developments have occurred in Soviet Russia and have been a source of maladjustment as between planned and actual outputs. The State Planning Commission

is, of course, in a position to control the rate at which technological changes will be introduced into industry. It could even shelve new inventions, as some capitalistic enterprisers do, until existing industrial equipment became almost completely worn out or until a given plan had been fulfilled. However, it would not be likely to do such things, especially since socialists are loud in their condemnation of such practices under capitalism and since the maladjustments in output which resulted from technological change would be in the direction of producing more rather than less than planned amounts. On the other side of the picture, the managers of enterprises under socialism, intent on producing the physical quantities of goods called for by the plans, might permit machinery and equipment to be abused or to receive improper and inadequate maintenance. In such cases, unforeseen breakdowns of machinery and equipment and stoppages of work might occur which would be disastrous from the point of view of fulfilling the plans.

Unexpected military needs may also interfere significantly with the fulfillment of economic plans. Of course, the Russian economic plans have always included anticipated military needs for war or national defense, and, in the case of an offensive war, the planners or Party leaders might be able to select the time and place of the adventure to suit themselves so that the necessary expenditures, changes in production, and shifts in personnel could be provided for to some extent. However, military needs and costs are always rather difficult to estimate and plan for in advance and, when a country such as Russia is suddenly called upon to protect herself against an attack by another power, we may be sure that the resulting war activities will profoundly upset her efforts to fulfill the economic plans of the period. Thus, even the minor war with Finland in 1939 and 1940 had a significant influence on the efforts of Russia to fulfill the Third Five-Year Plan and the serious effects of the more recent major war with Germany on the fulfillment of the same plan can scarcely be imagined.

Finally, we must note that the economic plans deal necessarily with the activities of millions of human beings, and human behavior is never precisely predictable. The planners may estimate that a certain number of workers, given certain supplies of machinery, land, equipment, materials, and power, will turn out a specific number of units of product of definite quality in a given period, but the results of the workers' activities may be anything but those which are ex-

pected. The adequacy of wages and working conditions, the effectiveness of non-wage incentives, the general health and welfare of the workers and their families, the presence or absence of economic security, family relationships, and many other factors affect the ability or the willingness of the workers to produce. It is small wonder that some of the greatest discrepancies between planned and actual results have occurred in connection with such matters as the productivity of labor, cost of production, and the numbers of workers required to achieve a given planned physical output.

The leaders of the Russian economy are conscious of the difficulties that bar the fulfilling of even the best laid plans and they struggle mightily to make the economy function according to plan. The State Planning Commission and all the functional and regional planning agencies have divisions whose duty is to see to it that the economic plans are fulfilled as nearly as possible, and they do their best to keep the managers of factories, farms, and other enterprises plan-conscious. However, it must be noted that the fulfillment of the plans in some respects may lead to their non-fulfillment in others. That is, the managers of factories, in their efforts to fulfill the plans with respect to physical quantities of goods, may fail to carry out the plans with respect to quality of goods, cost of production, or labor standards.

Partly because of the difficulties which may be encountered in carrying out the plans, it is customary to state the various objectives of the plans not as single figures but as ranges, at least at the beginning of a given Five-Year Plan. Thus the goal with respect to the annual production of steel at the end of a coming five-year period may be stated to be from 35 to 40 million tons. The planners also maintain running indexes which constantly show the relationship which exists between production (or other activities) in important interconnected phases of the plans. In this fashion, progress in the production of, for example, steel would be constantly observed in connection with the rate of growth in the production of automobiles, tractors, industrial machinery and other related branches of production. Any tendency for important related phases of the plans to get out of line with each other is quickly detected and, if possible, checked. Finally, the practice of revising the main plans by means of quarterly and annual plans is a recognition of the difficulties of plan fulfillment and an attempt to cope with these difficulties.

*The Contents of the Five-Year Plans* Before finishing this brief

**TABLE I**  
**SELECTED OBJECTIVES OF THE FIVE-YEAR PLANS  
 OF SOVIET RUSSIA**

Item	1928 Result	First Plan	Second Plan	Third Plan	Fourth Plan
<b>General objectives</b>					
National income (billions of rubles)	25 3	49 7	100 0	172 8	177 0
* Total new investment (billions of rubles cumulated through five-year periods)		64 5	133 4	188 2	250 3
Total industrial production (billions of rubles)	18 3	44 9	92 7	184 0	205 0
Output of producers' goods (billions of rubles)	8 2	21 0	45 5	114 5	137 0
Output of consumers' goods (billions of rubles)	10 1	23 9	47 2	69 5	68 0
* Total wage workers (millions)	11 4	15 8	29 6	32 0	33 5
Average wage (in rubles)	703	1231	1748	4100	6000
<b>Specific objectives in industrial production</b>					
Crude oil (millions of tons)	11 6	21 7	46 8	54 0	35 4
Coal (millions of tons)	35 4	75 0	152 5	243 0	250 0
Pig iron (millions of tons)	3 3	10 0	16 0	22 0	19 5
Steel (millions of tons)	4 2	10 4	17 0	28 0	25 4
Rolled steel (millions of tons)	3 4	8 0	13 0	21 0	17 8
Sawn lumber and timber (million cubic meters)	13 6	42 5	43 0	45 0	39 0
Automobiles and trucks (thousand units)	0 7	105	200	400	500
Locomotives (units)	478	1600	2800	2340	4000
Freight cars (thousand units)	10 6	12 6	118 0	120 0	
Railroad freight carried (billion ton-kilometers)	93 4	162 7	300 0	510 0	532 0
Electric power (billion kilowatt hours)	5 0	22 0	38 0	75 0	82 0
Cotton cloth (million meters)	2742	4588	5100	4900	4686
Woolen cloth (million meters)	96 6	270	220	177	159 4
Leather footwear (million pairs)	23 0	80	180	258	240
<b>Specific objectives in agricultural production</b>					
All grains (million metric quintals)	733	1058	1048	1300	1273
Raw cotton (million metric quintals)	8 2	19 1	21 2	32 9	31 5
Flax (million metric quintals)	3 2	6 2	8 0	8 5	9 3
Sugar beets (million metric quintals)	101 4	195 5	276 0	282 0	270 8
* Horses (million head on hand)	33 5	36 9	21 8	21 9	15 3
* Cattle (million head on hand)	70 5	80 9	65 5	79 8	65 3
* Sheep and goats (million head on hand)	146 7	160 9	96 0	170 7	121 5
* Hogs (million head on hand)	26 0	34 8	43 4	45 6	31 2

\* All figures except those marked with an asterisk are on a per-year basis

summary of economic planning in Soviet Russia, it will be well to examine the contents of the Five-Year Plans. We shall leave the discussion of the organizations, methods, and practices which have been developed in various fields of economic activity, and the results which have been achieved in the operation of the planned economy, to later chapters, and content ourselves here with observing the goals which the plans have set up. The statistics on the objectives of the four Five-Year Plans through 1950, as presented in Table 1, should be regarded as approximations, both because they were gathered from a considerable number of scattered sources and because of the constant revision of objectives which has gone on during the operation of each plan. The figures are given primarily to show the magnitude of the objectives undertaken by the Russian planned economy and can be adequately evaluated only in relation to the results which have been attained. In general, we shall find that some individual objectives have been almost exactly attained, that others have been overfulfilled, and that some have been far in excess of the results which could be achieved. This last result is indicated in some cases by the fact that the goals set up for the Second and Third Five-Year Plans have been smaller than those of the first plan. The relatively low objectives set up for many items under the Fourth Five-Year Plan reflect both the disruptive effect of World War II on the Soviet Russian economy and the disappointing results of trying to attain some of the more grandiose goals of the earlier plans.

*Resources of Soviet Russia.* Any failure to carry out the economic plans of the country can scarcely be charged to a lack of resources on the part of Soviet Russia. The U.S.S.R. has an area of some 8,400,000 square miles or one-sixth of the earth's land area. It stretches 6000 miles from east to west and 1800 to 2800 miles from north to south. Its population was estimated at 193,000,000 in 1945.<sup>6</sup> Russia has within her boundaries many different types of soil and most of the varieties of climate known to man and hence is able to produce practically all kinds of agricultural crops. It is only fair to say, however, that much of the land is none too good for agricultural purposes and that about two-thirds of the cultivated area of the country is found in the relatively small steppe region which contains only about 12 per cent of Russia's total area.<sup>7</sup>

<sup>6</sup> E. J. Simmons, editor, *U.S.S.R. A Concise Handbook*, p. 16.

<sup>7</sup> *International Conciliation*, April, 1948, p. 271.

<sup>7</sup> E. J. Simmons, *op. cit.*, p. 26.

Soviet Russia is very rich in natural resources. Her coal deposits are estimated at 1654 billion tons and are second only to those of the United States. Russia's reserves of petroleum, peat, and manganese are the largest in the world, and amount to 8640 million tons, 151 billion tons, and 785 million tons, respectively. Iron deposits are estimated at 11 billion tons, or about half the world total. Large though less spectacular deposits of copper, zinc, lead, gold, platinum, vanadium, molybdenum, tin, and bauxite are available. Potassium and magnesium salts are present in tremendous quantities, putting Soviet Russia first in the world as a producer of potash, and she has about 75 per cent of the world's known reserves of apatite. Timber reserves are also very large.<sup>8</sup> Of course, many of these resources are far from completely developed as yet.

### *Making Economic Decisions in Britain under Partial Socialism*

**Public Ownership and Operation** The British economic system, under the Labor Government, is intended to be one of partial socialism with only about 20 per cent of the economy under public ownership and operation. To the prewar examples of public ownership and operation, such as the Post Office and the British Broadcasting Company, the Labor Government had added only seven industries by the middle of 1949 (coal, banking, telecommunications, civil aviation, inland transport, electricity, and gas and coke). At the same time, nationalization of at least some sections of the iron and steel industry was in prospect. The industries brought under public ownership and operation were not selected haphazardly. They all seemed to have some or all the following characteristics:

- (1) They are of key importance to the economy, not only to ensure present production but to guarantee continual full employment, an objective on which all Parties are united.
- (2) They have not been fully efficient in the past, and need radical reorganization along the lines of a centrally operated plan. This means monopoly if left to private ownership, and they are therefore taken into public ownership.
- (3) They need large capital expenditure coming to a large extent either from the State or through State guarantee. If the State supplies funds it must be certain that they are spent for public and not private interests.

<sup>8</sup> *Ibid.*, pp. 28, 29.

- (4) They are already linked so closely with other Government operations that public ownership or control is a logical development.<sup>9</sup>

**Economic Planning** The economic powers of the Labor Government are in no wise limited to the operation of publicly owned industries, for it is the definite intent of this Government to have large-scale economic and social planning in postwar Britain. A part of the planning may never register with the average citizen, for much planning work consists in studying overall trends, in collecting and analyzing national statistics, and in making sure that satisfactory balances are being struck. In many fields of economic endeavor there may be nothing better to do, once the situation has been studied, than to allow events to take their course, for existing trends may be quite satisfactory, or as satisfactory as can be achieved under existing circumstances. However, the Labor Government is determined to go far beyond this analytical stage where necessary. It has a number of clearly defined objectives in mind for the country as a whole and, since the means for attaining these objectives were severely affected by the war, it realizes that a careful budgeting of resources will be required.

The short-run objective of economic planning in Britain is, of course, to devise ways and means of coping with the postwar economic emergency centering on such items as wartime destruction and loss of assets, inadequate production, unbalanced trade and the dollar shortage, and scarcities of consumers' goods. On the other hand, the long-run objectives of planning include "the permanent abolition of mass unemployment, the establishment of a complete system of social insurance and social security, the raising of the physical and educational standards of all the people, the ending of urban slums and rural decadence, and the development of beautiful towns, well-ordered farms, and a restful countryside."<sup>10</sup> The means for achieving these objectives will be studied in detail in later chapters.

The work of analyzing statistics, spotting trends far ahead, devising plans that can lead to manageable policies, and keeping the plans human and flexible is coordinated through an Economic Planning Board, which was set up after the coal-transport emergency of February, 1947. In developing the long-term plans for the

<sup>9</sup> British Information Services, *Labor and Industry in Britain*, September-October, 1947, p. 202.

<sup>10</sup> *Ibid.*, p. 156.

use of Britain's manpower and resources, the Board and its Chief Planning Officer work directly under the Lord President of the Council and have access directly to all Ministers (Cabinet members) concerned with production. However, major policy decisions with respect to planning are made by the Cabinet, not by the Planning Board or its Chief Planning Officer, and responsibility resides wholly with the Ministers. It is merely expected that the Cabinet will be greatly assisted by having at its service a Planning Board devoted to considering planning issues, with free access to materials in all governmental departments, and unburdened by ordinary departmental duties.

*The Position of the Individual.* According to the announced intention of the Labor Government, economic planning is intended to provide only the broad framework for the development of the British economy. Within this framework, it is supposed to be left to private individuals to carry out the plans and to conduct a great part of their business and all their leisure activities according to their individual talents and tastes. This may, of course, turn out to be the actual situation in the long run, but for the present the Labor Government seems to rule the British economy with an iron hand. Almost every type of economic control known to the mind of man is at the disposal of the government, and practically every type is in actual use. Under rigid governmental controls affecting virtually all phases of economic life, private ownership and operation of industries and businesses means very little and economic freedom for the individual is a joke. It still remains to be seen whether the present situation will carry over into the long run.

### *Making Economic Decisions under Fascism*

*The Early Situation.* As we have seen, the operation of fascist economic systems in Italy and Germany involved no change in the nominal character of the economic institutions of these countries. The fascist leaders, in other words, professed great admiration and respect for private property, free enterprise, individual initiative, and competition, and proposed to rely on these capitalistic institutions for the operation of the economic system so far as this course of action produced desirable results. However, the goals of the state or nation were to be supreme, and, if the operation of capitalistic institutions tended to produce results which were inconsistent with

state objectives, the government would have to step in with appropriate interferences and controls.

The fascist leaders declared repeatedly that they did not intend to set up an economic system like that of Soviet Russia, in which the state owns and operates the basic means of production, and individual initiative is weakened if not destroyed. Indeed, the system was not intended to be permanently even a governmentally controlled system. The government did not propose to direct industry and trade in the long run, but intended merely to open up the way for private industry and trade. Many of the early policies followed by the fascist governments were of a sort calculated to be popular with business men. Labor unions were suppressed, strikes eliminated, consumers' and workers' cooperatives discouraged, and wage rates lowered by governmental decree. Then followed the reprivatization of industries governmentally or municipally owned, the substitution of sales taxes for business income taxes or the removal of taxes on capital issues, the erection of higher tariff walls, and direct subsidies to industry.

Under such conditions, Italy enjoyed a period of great prosperity from 1922 to 1927. Production in general increased by more than 50 per cent during the period, with the increase being particularly great in the production of durable goods. The production of iron and steel increased to nearly double its 1913 level, the output of motor cars amounted to one-eighth of total European production, shipbuilding and hydroelectric power production advanced to several times their prewar levels, and Italy became the largest European producer and the world's largest exporter of rayon. The industries producing chemicals, rubber goods, and machinery expanded rapidly. Italian foreign trade grew by leaps and bounds and was 90 per cent greater in 1926 than in 1922. New investments in corporate enterprises amounted to 2 billion lire in 1923, 5 billion lire in 1924, and 8 billion lire in 1925. The stock market was active, the volume of unemployment was insignificant, and the net earnings of industry increased from 17 per cent of invested capital in 1922 to 8 per cent in 1925 and 7 per cent in 1926.<sup>11</sup>

However, this boom period, as is so often the case, contained the seeds of its own destruction. The distribution of income in Italy was such that the rapidly growing quantities of industrial products

<sup>11</sup> C. T. Schmidt, *The Corporate State in Action*. New York: Oxford University Press, 1939, pp. 117-118.

could not be taken off the market at home, and Italian industries had obviously overestimated the possibilities for developing export markets Some Italian industries were relatively high-cost producers, for they were not as efficient as industries of the same type in other countries, and the problem of excess capacity arose in the rayon, sugar, chemicals, shipbuilding, and other important Italian industries

Finally, the Fascist government helped to bring the boom period to an end when, at the end of 1927, it stabilized the lira at the rate of 19 to the dollar This value set on the lira was high in relation to what its value had been in the years since World War I, and stabilization at this artificially high rate, while favorable to the prestige of the Fascist regime and to the interests of persons living on fixed incomes from property, ran counter to the interests of business men and bankers It made for falling prices, decreased business activity, and a relative increase in the burdens of debts The artificially high value of the lira in terms of gold made the prices of Italian goods seem high in relation to the prices of the same goods in other countries and the Italian export trade was hard hit Business failures increased rapidly

By 1932, production was 25 per cent below the 1928 level and about a third of Italian productive facilities became idle Italy's foreign trade in commodities declined about two-thirds from the 1926 level and her income from the so-called invisible items of international trade fell by 60 per cent Corporate capital was written down by 16 billion lire and industrial earnings fell from 6 per cent on invested capital in 1928 to 0.6 per cent in 1931 and -10 per cent in 1932 Business failures increased from 7600 in 1926 to an annual average of 12,000 from 1929 to 1933 Over a million Italian workers became unemployed, and the national income declined one-third from 1928 to 1931<sup>12</sup>

*The Development of Governmental Control in Italy* These depressed conditions in the Italian economy led to a considerable extension of governmental controls The government greatly enlarged its public works program, the length of the work week was reduced in order to spread the work, and the internal migration of workers was severely controlled The government required the citizens to surrender all foreign credits and securities in exchange

<sup>12</sup> *Ibid.*, pp. 119-120

for government bonds in order to support the lira Tariffs were raised until they became the highest in the world, and rigid quota controls, import licenses, export subsidies, and bounties were applied More taxes were shifted to consumers through the use of sales taxes

The *Istituto Mobiliare Italiano* and the *Sofondit* began to use government credit to support the credit of private business firms That is, these agencies extended credit to private firms in return for the stocks and bonds of these enterprises, and then issued their own bonds, guaranteed by the government, in order to recover their funds They also took industrial securities off the hands of the banks in similar fashion The *Istituto di Ricostituzione Industriale* was set up in 1933 to look after the financial reorganization of business firms, to liquidate bankrupt firms, and to furnish financial aid to business enterprises by means of long-term loans financed ultimately by the sale of government-guaranteed bonds In spite of all these measures, Italian recovery from the depression was far from satisfactory

Later on, as the depression was followed by the war with Ethiopia, and preparation for and eventually participation in World War II, Italy developed steadily into a completely controlled economy, and the power to make the basic economic decisions passed from the hands of business men and firms, where it had formerly resided, into the hands of governmental officials and agencies The ultimate power to make economic decisions was possessed, of course, by Mussolini and a small handful of party leaders, but much of it was delegated to various governmental agencies The most important of these was the Ministry of Corporations, one of the departments of the Italian government, which was entrusted with a wide range of duties in connection with the supervision and control of economic activities and did a great deal of the economic planning for the country Other important agencies were the Central Corporate Committee, composed of a number of government Ministers, high party officials, and officials from lower control agencies of the government, and the National Council of Corporations, which included the Central Corporate Committee and a large number of delegates from the category corporations (governmental organizations for the control of production) With these organizations functioning, private business men and firms

could hope to affect the making of basic economic decisions only through such influence as they might have with party and governmental officials and agencies.

*The Development of Governmental Control in Germany* The National Socialist Party came into power in Germany more than ten years after the Fascist Party had seized control in Italy. It had a severe business depression to cope with immediately, and it did not wait long before starting to interfere with and control the economic life of the country. On May 1, 1933, the First Four-Year Plan was announced. This plan was not one covering the general functioning of the economy, but was supposed merely to deal with the abolition of unemployment. Among the measures included in the plan were public works, subsidies to private building operations, rebates of taxes on renewals of industrial equipment, work-spreading, the absorption of workers outside the ordinary fields of production by means of the labor service, the "land-year," marriage loans, and tax remissions for female domestic servants, restrictions on dismissals; subsidies for the employment of older workers, especially those with large families, the prohibition of "multiple earnings" within the family, the reintroduction of universal compulsory military service, the payment of bonuses to newly married couples if the wife agreed not to resume employment, and, eventually, the great rearmament program.

By the fall of 1936, the unemployment problem had virtually disappeared, and Germany embarked on the Second Four-Year Plan. This plan, like the first one, dealt with a specific problem and did not cover all details of economic activity. Its purpose was to further the program of preparing for war by making Germany independent with respect to all foods and raw materials necessary to the effective conduct of war. The work of the plan was organized under six general divisions, each headed by a staff of army officers and big business men. The specific aims of the plan were said to be to increase the output of raw materials, to distribute all raw materials, and especially iron and steel, so that the armaments industries and other key industries would be able to attain their objectives, to distribute labor with especial regard for the needs of military and economic armament industries, to increase agricultural production in general and especially in those lines which produced raw materials for industry, to keep prices and wages stable, and to

control and distribute foreign exchange.<sup>13</sup> We shall look into the methods for achieving national economic self-sufficiency in some detail in a later chapter.

*General Economic Planning* During the periods of the Four-Year Plans, many phases of German economic life were brought under rigid governmental control. The Labor Front was organized and many offices and agencies for the control of employer-employee relationships were established. The so called Estates of Industry and Trade, Handicrafts, Transportation, and Agriculture were created for purposes of governmental control in these particular fields. The government organized controls over prices and wages, international trade, credit and investment operations, and other things. Through all this extension of governmental powers, Germany seems to have developed economic planning in the Italian, rather than the Russian, sense.

Until the Second Four-Year Plan came into active operation, the most important economic decisions seem to have been entrusted to the Minister of Economic Affairs and his immediate advisers, under the general supervision of the Party leaders as a whole. Later, there was considerable duplication and overlapping of functions as between the leaders of the Ministry of Economic Affairs and the authorities at the head of the Second Four-Year Plan, and the Ministry of Economic Affairs was reorganized. In January, 1940, General Goering and an advisory council were placed in charge of all German economic activities, including the jurisdiction of private business, the war department, and the government, while the Minister of Economic Affairs was definitely placed in a subordinate position. The advisory council included the following officials "state secretaries representing the Ministries of Economic Affairs, Labor, Transportation, Interior, Reich-Forest Office, and the Four-Year Plan, a delegate from the Nazi Party, and the chief of the war economy office of the High Command."<sup>14</sup>

Thereafter, this General Council for the War Economy and its leader were apparently in charge of making for Germany many comprehensive economic decisions of the type which we have been discussing in the present and preceding chapters, even though the

<sup>13</sup> M. Y. Sneezy, *The Structure of the Nazi Economy* Cambridge Harvard University Press, 1941, pp. 21-22.

<sup>14</sup> *Ibid.*, p. 53. Reprinted by permission of the President and Fellows of Harvard College.

group may not have been dignified with the title of State Planning Commission. Of course, the ultimate power of decision making, in the economic sphere as in others, lay in the hands of Hitler and his immediate associates. It was also true that some important business men and industrialists had a great deal of influence with high party and governmental officials and may have been able to affect in some measure the economic decisions which were ultimately reached.

**Conclusion on Planning** There can be no doubt that the fascist countries, at least in their later years, operated on the basis of economic planning of a sort. That is, the most important and comprehensive economic decisions—those involving the kinds and quantities of goods to be produced, the allocation of the productive agents, the distribution of consumable goods, and the balance between spending and saving—were made by the leaders of the ruling party and the government and not by private individuals on the basis of price relationships. On the other hand, there seemed to be in each country no definite and continuously functioning body, known as a State Planning Commission, which was charged with the duty of making economic plans; there was little indication that detailed plans were drawn up for all departments of economic activity for several years at a time, with supplementary detailed estimates of proposed achievements in individual years; there seemed to be no provision for public participation in the process of planning; the exact identity of the individuals who did all the planning was not always clear, and the ownership of productive wealth and the detailed operation of economic activities seemed to be left in the hands of private individuals for the most part.

There is little indication that any attempt was made in either Italy or Germany to adapt the operation of the economy to the actual or supposed wishes and desires of the citizens as private individuals. The leaders of party and government realized that the citizens would have to be provided with certain minimum amounts of necessities and comforts in order that they might be able to function efficiently in serving the ends of the state, but that was all. Apart from this consideration, the leaders did not care what the desires of the citizens may have been and made no effort to fulfill them. Only the interests of the state or nation were deemed worthy of serious consideration.

**Fascist Resources** Although economic plans can be made and, if reasonable, fulfilled whether an economy's resources are plentiful

and high grade or limited and low grade, it must be said that the fascist leaders, as economic planners, had comparatively little with which to work. With a land area of only 119,000 square miles and a population of about 44,000,000, Italy had to support a population over a third as large as that of the United States on an area about three-fourths as large as our state of California. Some of the land was not suitable for cultivation and much of the land in use was of rather poor quality and badly worn. From the point of view of industrialization, Italy was sharply deficient in such important materials as coal (83 per cent imported), petroleum (91 per cent imported), iron ore, chrome (98 per cent imported), copper 89 per cent imported), tin (98 per cent imported), nickel (virtually 100 per cent imported), manganese (55 per cent imported), cotton, wool, and many other materials. Such deficiencies could not be offset by having a sufficiency of aluminum, zinc, lead, mercury, sulphur, marble, and water power, and a fair amount of timber. The task of making Italy prosperous is a most difficult one under economic planning or any other system.

The German economy was but little better off than the Italian system in the matter of resources. Before the incorporation of Austria in the German Reich, Germany had a population of 66,000,000, or about half that of the United States, living on an area of 181,000 square miles, or an area about 15 per cent larger than that of our state of California. Before the self-sufficiency program bore its expensive fruit, Germany was dependent on imports for about 20 per cent of her food supply. From the point of view of industrialization, she had ample supplies of coal, potash, and magnesite, shortages of antimony, iron ore, lead, manganese, rubber, petroleum, sulphur, timber and wood pulp, and zinc, and major shortages of asbestos, tin, tungsten, and vanadium. The self-sufficiency program eliminated a part of this dependence on foreign countries, though at terrific cost. Germany's conquests in World War II added greatly to her land area, population, and resources, but all this did no good when she was unable to hold these gains.

#### QUESTIONS

- 1 "All important economic decisions would be made without reference to price relationships under communism" Explain
- 2 "The Russian economic system did not change from capitalism to a planned economy overnight" Explain

- 3 "The Russian State Planning Commission receives a great deal of help with its work of economic planning" Discuss
- 4 Explain the method which is used in formulating a Five-Year Plan and placing it in operation
- 5 "The economic results planned by the State Planning Commission in Russia are likely to be better suited to the basic needs and desires of the citizens than the results achieved by capitalism on the basis of the price system would be" Do you agree? Explain
- 6 "Economic planning in Soviet Russia produces a completely controlled economy, that is, the economic plans, whether they are good or bad, can always be fulfilled" Show whether you agree
- 7 "Even though economic plans are made very efficiently and accurately in Soviet Russia, it is too much to expect that these plans will ever be perfectly fulfilled" Why?
- 8 How do the Soviet Russian planners attempt to keep their Five-Year Plans "balanced and flexible"?
- 9 "The goals set up by the Russian Five-Year Plans to date have been highly optimistic" Show whether you agree
- 10 "Any failure to carry out the economic plans can scarcely be charged to a lack of resources on the part of Soviet Russia" Discuss
- 11 On what bases have certain industries been selected for nationalization in Britain under partial socialism?
- 12 How is economic planning carried on in Britain under partial socialism, and what are its short-run and long-run objectives?
- 13 "The individual business man will probably be affected very little by economic planning in Britain under partial socialism" Discuss
- 14 "The fascist economies of Germany and Italy only gradually came to operate on the basis of economic planning" Explain
- 15 "During World War II, it was certainly accurate to refer to the fascist systems of Germany and Italy as fully planned economies" Do you agree? Explain
- 16 Compare economic planning in the fascist countries with that which is carried on in Soviet Russia
- 17 "The economic planners of Germany and Italy under fascism did not have very adequate material resources with which to work" Explain

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**CHAPTER 7**

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**THE ORGANIZATION OF  
PRODUCTION*****The Organization of Production under Capitalism***

As we have seen, productive wealth is privately owned for the most part under capitalism and productive enterprises are operated by private individuals. Moreover, a capitalistic society is willing, on the whole, to accept as appropriate whatever total productive results are produced by the reactions of private individuals on the basis of price relationships. Under these conditions, the government of a capitalistic system does not, except perhaps in times of great emergency, set up large and elaborate organizations of its own for the purpose of controlling and coordinating productive activities in general. While the various forms of the business unit (such as the corporation or partnership) which private individuals use under capitalism are subject to various laws and regulations, individuals are ordinarily quite free in the matter of selecting the form of the business unit which is best suited to their particular enterprises.

***The Forms of Private Enterprise*** In the capitalistic system of the United States, most business enterprises are set up as single proprietorships, partnerships, or corporations, and the corporation is, on the whole, far more important than the other forms of the business unit. In 1939, according to the Bureau of the Census, United States Department of Commerce, corporations made up 51.7 per cent of the total number of enterprises in manufacturing, but they employed 89.4 per cent of the workers, turned out 92.6 per cent of the total value of manufactured products, and were responsible for 92.3 per cent of the total value added by manufacture. In the economy as a whole there were only a little over 400,000 corporations out of more than 3,000,000 operating business firms in

1945, but the corporations produced 87 1 billion dollars and single proprietorships and partnerships only 44 2 billion dollars out of a total of 142 3 billion dollars of national income originating in business<sup>1</sup>

The importance of the corporation itself varies greatly from one field of productive activity to another. Corporations in 1939 made up only 0 14 per cent of all enterprises in agriculture, 4 87 per cent in retail trade, and 7 47 per cent in construction, but went up to as high as 63 per cent in the extraction of minerals.<sup>2</sup> In 1937, corporations were responsible for only 7 per cent of the total income produced in agriculture, and only 30 and 36 per cent of the income produced in the construction and service fields. On the other hand, corporations produced 89 per cent of the total income in the field of transportation, 92 per cent in manufacturing, 96 per cent in mining, and 100 per cent in communications, and electric light and power and manufactured gas. The average for all branches of production was 60 to 65 per cent.<sup>3</sup>

In addition to single proprietorships, partnerships, and corporations, cooperative enterprises play a small part in productive activities under capitalism. Cooperative enterprises have not attained a high level of development in the United States, and yet in 1944 there were approximately 4300 retail cooperative associations in this country, with a total membership of more than 1½ million persons and a gross volume of business amounting to \$557,000,000. In the same year there were also 577 service cooperatives (providing housing, medical care, or burial service), 850 electricity associations, 5000 telephone associations, 9000 credit unions (or financing organizations), and 2000 insurance associations. However, the volume of business done by cooperatives of all sorts was an exceedingly small fraction of the total for the country as a whole.<sup>4</sup>

**Large-Scale Production and Combination.** Productive activities in the United States over the last several decades have been char-

<sup>1</sup> *The Economic Almanac for 1946-47*. New York: National Industrial Conference Board, 1946, pp. 90-91; W. N. Peach and Walter Krause, *Basic Data of the American Economy*, Chicago: Richard D. Irwin, Inc., 1948, p. 177.

<sup>2</sup> *The Economic Almanac for 1946-47*, p. 93.

<sup>3</sup> Temporary National Economic Committee, Monograph Number 20, *Taxes, Recovery, and Defense*, Washington: Government Printing Office, 1940, p. 319.

<sup>4</sup> *The Competition of Cooperatives with Other Forms of Business Enterprise*, House Report No. 1888, Washington: Government Printing Office, 1946, pp. 26, 27.

acterized not only by the rise of the corporation to a position of dominance as a form of the business unit but also by the growth of large scale production and the development of business combinations. Firms with an annual product valued at a million dollars or more included only 2.2 per cent of the total number of firms in manufacturing in the United States in 1911, but these few large firms employed 35.3 per cent of all workers in manufacturing and turned out 18.7 per cent of all manufactured products by value. In 1937, the plants with an annual product valued at a million dollars or more included 6.0 per cent of all plants in manufacturing, employed 57.9 per cent of all manufacturing workers, and produced 70.4 per cent of all manufactured products by value.<sup>5</sup> In all fields of economic activity in the economy, large scale business units amounted to 7.5 per cent of the total number, but employed 55.2 per cent of the personnel and contributed 65.9 per cent of the total value of output.<sup>6</sup>

In many cases, the expansion of the productive unit does not stop with simple large-scale production but goes on to the formation of combinations of productive establishments. The majority of the many thousands of business combinations in the United States are of the simple horizontal type. That is, they involve the union under one central management of two or more plants which turn out exactly the same product or products. Other combinations are of the vertical type, which involve the union under one central management of two or more establishments which operate in different stages of the process necessary to prepare the final product for the market, or of the complex horizontal type, whose two or more plants under one central management turn out unlike but not successive products. Finally, we may note that productive establishments in the United States usually employ roundabout and highly specialized methods of production.

*Governmental Influences.* Even though the government of a capitalistic country does not specify any particular forms in which pro-

<sup>5</sup> *Statistical Abstract of the United States, 1937*, p. 739, *The Chicago Tribune*, 1939.

<sup>6</sup> *The Economic Almanac for 1946-47*, p. 91. For this computation, large scale establishments were taken to be manufacturing plants with more than 100 employees, wholesale establishments with more than a \$200,000 annual sales volume, and retail stores, service establishments, hotels, places of amusement, and construction establishments with annual net sales or receipts of more than \$50,000.

ductive enterprises must be organized, it may discriminate against certain types of productive organizations. Thus, if it is apparent that the use of holding companies in certain fields is filled with abuses and unfortunate practices, the government may regulate the use of this form of organization or even prohibit its use altogether in certain cases. In any case, the fact that the government does not actively control the forms in which productive enterprises are organized does not mean that it may not engage in many activities which will affect the results of productive operation. Some governmental activities, such as the construction of canals or harbor facilities, the provision of a system of weights and measures, or the establishment and maintenance of a monetary system, are concerned primarily with the general development of economic activity. In other cases, as for example when the government undertakes to define and prohibit the use of unfair competitive practices, it is engaged in laying down general rules according to which private enterprises must play the game.

By means of such a policy as that of maintaining a high protective tariff, the government may influence not merely the course of international trade but the relative development of industry and agriculture, or that of different phases of industry, within the economy. If the private operation of economic activity leads to the formation of monopolies and the exercise of monopoly powers to the detriment of the public, the government may provide and attempt to enforce anti-trust legislation. If the operation of individual industries under private auspices produces serious evils and abuses, as in the case of the railroads and other public utilities, the government may bring these industries under close regulation and control. The government may establish plants of its own to serve as yardsticks for testing the efficiency of private concerns and the fairness of their pricing policies. Finally the government, even under capitalism, may decide to own and operate certain industries altogether. As we noted in Chapter 3, the governments of various capitalistic economies have owned and operated plants or industries for the production of an enormous variety of commodities and services, and have brought many other fields of production under governmental supervision and regulation.

In times of emergency, the government of a capitalistic economy may greatly expand the range of its activities and may interfere in the economic life of the country to a much greater extent than

usual For example, in the great depression after 1929, the federal government of the United States attempted to control a considerable range of economic activities, including especially the results of productive activities in agriculture (by means of the AAA) and in manufacturing and commerce (by means of the NRA) Again, during World War II, the federal government undertook to stimulate the production of certain types of goods greatly, to stop the production of other commodities completely, to allocate available productive resources among industries or firms, to control prices and wages, to stimulate individual saving so that large quantities of war bonds could be sold, and even to ration finished economic goods among the individual consumers However, these types of interference and control have to do with the kinds and quantities of goods to be produced, or other basic and comprehensive economic decisions, rather than with the organization of production as such

### *The Organization of Production under Socialism*

*The Continuation of Familiar Organizational Forms* Under socialism, as the ideal system is visualized by members of the socialist movement, land and capital would be publicly owned for the most part and most productive enterprises would be operated by the government in the name of the entire social group However, the organization of production which would probably result would not seem very unfamiliar to us If the corporate form of business organization has significant advantages from the point of view of operating efficiency, there seems to be no reason why the governmental enterprises which would dominate most fields of economic activity under socialism could not be organized as governmental or public corporations Such corporations could have all the usual officials and managerial methods and devices They could be managed by boards of directors as they now are, except that such boards would probably contain representatives of workers and consumers as well as those of management, and their duties would involve only the taking of the steps necessary to give effect to the economic plans of the system rather than the making of basic economic decisions and the determination of fundamental policies If combinations of productive units of any kind have genuine advantages from the point of view of efficiency, they could be set up and used as well under

socialism as under capitalism Production under socialism could be as roundabout, large-scale, and specialized as under capitalism

Most socialists do not think of their ideal system as one in which all types of production would be controlled and operated exclusively by public enterprises It is clear that there are some branches of personal service and petty production, as well as some activities of a highly individualized nature, which are not well suited to operation by public enterprises Thus, cooperative societies or even private individuals might be permitted to operate small restaurants, tea rooms, garages, filling stations, shops for repairing shoes, radios and many other things, tailoring, dressmaking, and shoemaking establishments, and shops for selling home-made cakes, cookies, preserves, pickles, and other products Some socialists would go even farther and say that all handicraft production, all or most agricultural production, all or most retail merchandising, and even some small manufacturing enterprises might safely be left to cooperative associations or private individuals<sup>7</sup> In general, these are fields of production in which the abuses or wastes of capitalism are thought to be at a minimum and which do not lend themselves especially well to operation by large-scale state enterprises

*Controlling Private and Cooperative Production* There would probably be no great harm in leaving a fair range of economic activities to cooperative associations and private individuals under socialism The private and cooperative enterprises could be made to bear costs comparable to those of governmental enterprises in other fields and several devices are available by means of which the government could control the productive activities of private and cooperative enterprises so as to keep their results in harmony with the economic plans for the whole system That is, the government could encourage production in some cooperative and private fields and discourage production in others by varying the prices set upon the finished commodities and services, by discriminatory taxation, by varying the interest rate charged for funds obtained from governmental financial institutions, by being willing or unwilling to advance funds in the first place, by issuing discriminatory rations to different types of producers, or by varying the goods available in

<sup>7</sup> On these matters, see H D Dickinson, *Economics of Socialism*, pp 166 172, H W Lander, *American Socialism*, pp 156 163, or John Strachey, *How Socialism Works*, pp 65 73



*The Organization of Production in Soviet Russia*

**The Ministries** As we have seen, the Ministries of Soviet Russia are usually both departments of government and departments of economic activity and are therefore important connecting links between the government and the economic life of the country. Until 1939, production in the Russian system was organized under a comparatively small number of Ministries. Transportation and communication were under the Ministries of Railroad Transportation, Water Transportation, and Communications. The Ministry of Internal Trade had control over all retail and wholesale marketing of finished goods, that of Finance operated most of the credit facilities of the system, and that of Foreign Trade controlled importing and exporting. Agriculture was under the Ministry of Agriculture and the Ministry of State Farms, while industry or manufacturing was dominated by the Ministries of Heavy Industry, Light Industry, Timber, Machine-Building, and Food. Since most other phases of economic activity will be covered in separate chapters, we shall be concerned here primarily with the organization of industrial production.

The Ministries in charge of industrial production did not actually produce anything, of course, but were merely control groups or administrative agencies. Each one was in charge not of a single industry but of a whole group of related industries. Thus, until 1939, the Ministry of Heavy Industry included the industries producing coal, coke, peat, petroleum, iron and steel, iron and manganese ore, copper, gold, aluminum, lead, zinc, nickel, tin, chemicals, cement, building materials and technical glass.<sup>9</sup> Clearly many other agencies and organizations below the level of the Ministries were needed for the detailed administration and supervision of industrial production.

**The Administrations** Each industry or branch of production under one of the Ministries was placed in the power of another control group known as an "administration" or "combine." Most of the powers of each administration were rather broad and supervisory in character. Some of them, such as the collection of reports and information, the supervision of accounting methods, the carrying on of research work, and the training of specialized personnel, were of the type which trade associations might carry on in some other

<sup>9</sup> *Russian Economic Notes*, Number 13, pp. 10-12.

economic system Other functions included the working out of plans for, and supervision of the construction of, new productive facilities (subject to the general economic plans), appointing and dismissing the officials of the next lower units of the industrial organization, deciding the uses to which the "profits" of the lower units should be put, supervising the purchase of raw materials and supplies and the sale of finished products for their industries, and the levying of fines and penalties on the lower industrial units

*The Trusts* Under each administration, several "trusts" ordinarily appeared These units were also control groups and may be compared with the combinations of productive units with which we are familiar in the United States Some of these trusts were vertical combinations of productive units, while others were horizontal combinations at given levels of production Some trusts had only plants which were concentrated in a single limited geographical area, while others had plants which were scattered over a much larger area The functions of the trusts were, in general, more detailed than those of the administrations Each trust was operated by a board (appointed by its administration) and this board in turn appointed the managers of the actual producing plants or factories Each trust was responsible for the productive equipment furnished to the individual factories by the state The trusts were to see that their plants interchanged technical experience and made use of results obtained by scientific and technical institutes, laboratories, and research organizations, to furnish their plants with information concerning technological advances in industries abroad and get their plants to adopt similar devices and improvements, to see that the plants made full use of their resources and kept stocks of materials, supplies, and finished products in proper amounts and under satisfactory conditions, to set up an orderly system of accounts and records within their plants, to see that the plants went as far as they should in standardizing their products, to supervise the wage contracts which the plants negotiated with labor organizations, and to purchase raw materials and sell finished products for their plants

*The Factories* Finally, under the trusts, we came to the individual plants or factories in which the commodities were actually produced The director of each enterprise was appointed by its trust, as noted above Within the enterprise, there were shops having managers in charge, sections of workers under the direction of foremen, and brigades of workers under brigade leaders While the offi-

cials in charge of individual plants or factories were to make the decisions necessary to the day-to-day operation of their establishments, it is clear that there were not many things left for these officials to decide. Each enterprise operated under very definite assignments derived from the economic plans of the system. Among the factors which were controlled quite specifically from above were the kinds and quantities of goods to be produced, the quality of the goods, the prices at which the goods could be sold, the quantities and qualities of productive factors which could be used, and the amounts to be paid for materials, supplies, labor costs, taxes, and other expenses. About the only things left to the management of the enterprises were routine decisions of everyday operation necessary to the carrying out of the plans, and the hiring and firing of labor. Even in such matters of routine factory operation, the managers were required to consult with the leader of the local unit of the Communist Party and a representative of the local labor unions. Where these worthies were both members of the Communist Party and the managers were not, it is to be supposed that the managers were relatively powerless to make even routine decisions with regard to the operation of their enterprises. At any rate, it is clear that decision-making within the local productive unit was in the hands of a triumvirate (manager, Party official, and labor representative) called the *Trioika*.

Although the powers of the manager were extremely limited, he was nevertheless held responsible for the successful operation of the enterprise and the fulfillment of its plans. If unsuccessful, he might be severely punished. With prices, costs, and quantities of productive agents so closely controlled, about the only factor which the manager could hope to influence was productivity or efficiency. That is, the manager was supposed to get his costs of production per unit of product down to the planned level by inducing an increase in the productivity of his enterprise, as compared with the preceding period, to the extent prescribed by the plan. If he could spur his workers on to the planned feats of productivity, his enterprise came out even or made "planned profits," as the case might be. If he induced feats of productivity greater than those which had been planned, he made "unplanned profits" and was a most successful enterpriser. However, as we have seen, a socialized economy and its people cannot get rich by making money profits,<sup>10</sup> and the profits

<sup>10</sup> See Chapter 1, p. 18.

were important primarily as an indication of the degree of efficiency achieved by the various enterprises and their managers. With great responsibility, limited powers, and no very great rewards for carrying on the occupation, it is not easy to see why many people would have aspired to be managers in Soviet Russian industry.

*Later Changes.* This organization of government owned and operated industry has been changed considerably in recent years. Beginning in 1939 there was a general reorganization of Soviet Russian Ministries and those in charge of industrial production were divided and subdivided. By 1945, the Ministries dealing with industrial production included Armaments, Automobile Industry, Aviation Industry, Chemical Industry, Coal Industry of the West, Coal Industry of the East, Construction and Roadbuilding Machinery, Electrical Industry, Ferrous Metallurgy, Fuel Industry Construction, Heavy Industry Construction, Heavy Machine Building, Machine and Instrument Construction, Machine Tools, Military and Naval Construction, Non-ferrous Metallurgy, Oil Industry of the South and West, Oil Industry of the East, Paper and Cellulose, Power Stations, Railroads, Rubber, River Transport, Shipbuilding, Transport Machine Construction, Building Materials, Cinematography, Fishing, Food Industry, Light Industry, Textile Industry, Timber Industry, and Radio Industry.<sup>11</sup>

With many of the Ministries coming to include only a single industry, rather than a large group of industries, it seems clear that the old control agencies called administrations, which were also at the head of single industries, are no longer a necessary part of the industrial organization. In some cases "departments" or "production territorial sections" are the new control agencies operating under the Ministries. These agencies are committees heading up the lines of production of a given branch of industry and controlling a given territory.<sup>12</sup> In these Ministries the trusts and individual plants underlie the departments or sections. The departments have wide powers for controlling the productive activities of trusts and factories, furnish supervision and guidance to these lower industrial units on a number of technical and financial matters, and are responsible for getting raw materials and supplies to the lower units and for selling their products. However, there are no sections or

<sup>11</sup> *The Soviet Economy Today*, p. 26.

<sup>12</sup> *Soviet Russia Today*, February, 1948, p. 23.

departments under some Ministries, and in such cases the trusts are responsible directly to the Ministries.

In 1937, the Troika, or triumvirate for making various initial enterprise decisions, was abolished, and the managers or directors of enterprises were given more authority in the operation of their establishments. It is not certain whether this development resulted from a recognition of the need for greater power on the part of the managers or merely from the fact that more and more of the managers were becoming members of the Communist Party who could be trusted to function with less supervision than formerly. In any case, however, the position of a manager is still anything but a rosy one. All these changes suggest that the industrial organization of Soviet Russia is extremely flexible and subject to continuous reorganization on a rather costly trial and error basis.

*Government Ownership of Industry.* The ownership and operation of industries by various governmental units in Russia corresponds rather closely to the prospectus given out by modern socialists. Ministries, such as those of the Automobile Industry, Aviation Industry, Chemical Industry, Coal Industry, Electrical Industry, and many others, are All-Union Ministries, and the various enterprises under their supervision are owned and operated by the federal government through these Ministries. On the other hand, such Ministries as those of the Fishing Industry, Food Industry, Light Industry, Textile Industry, and Timber Industry, are Union-Republic Ministries, and the various enterprises under their supervision are owned and operated by the republic governments (or lower governmental units) through these Ministries. Finally, some enterprises of local interest, such as various public utilities, are owned and operated by local governmental units or Soviets.

*Cooperative Production in Industry.* The extent of cooperative production in the socialized economy of Soviet Russia also bears out fully the claims of modern socialists in this matter. As we shall see later, over 90 per cent of the cultivated area of Soviet Russia is in the hands of collective or cooperative farms, and various estimates hold that these cooperative farms include some 19 to 22 million peasant households or families. There are also some three million persons in various other producers' cooperatives. Narrowing the field still further to our present interest of industrial production, there were about 1,500,000 hand workers in various industrial (or handicraft) cooperatives in 1937. These producers' cooperatives

turned out a total product valued at 13,178 million rubles in 1937, as compared with one worth 5,764 millions in 1932. They were said to be responsible for about 20 per cent of the market supply of consumers' goods, including 35 per cent of the furniture, 40 per cent of the metal goods, 67 per cent of the metal bedsteads, 33 per cent of the felt footwear, and 50 per cent of the knit overgarments, peasant art goods, embroideries and laces, scissors, kerosene pressure-stoves, and wooden and other toys.<sup>13</sup>

In 1940, the products of the industrial cooperatives increased by 15 per cent over 1939, and new investments of 550 million rubles were made in these establishments. Then output was expected to reach 19 billion rubles in 1941, including 15 billion rubles' worth of consumers' goods. Among the specific items included in this total were 40 million pairs of footwear, 78 million meters of cotton textiles, 61 million pairs of socks and hose, 25 million knitted outer garments, 47 million sets of knives, forks, and spoons, 150 thousand phonographs, and 570 thousand kerosene stoves.<sup>14</sup> The producers' cooperatives were praised for having developed many "new" products such as heat-resisting ceramic ware, home mechanical refrigerators, drying drums for laundry, rubber goods, artificial stone, chemical products, paints, cardboard, leather goods, and metal substitutes. They had also achieved considerable success in repair work in connection with shoes, clothing, and household utensils. On the other hand, they were criticized for shortages of toys, hose, school supplies, and barber, laundry, and photographic services.

This emphasis and dependence on cooperative production has carried over into the postwar period. Faced with continuing shortages of consumers' goods, the Council of Ministers of the USSR in 1946 took several steps to encourage production by cooperatives. A large government loan and government materials and equipment were placed at the disposal of the cooperatives and they were relieved of the necessity of filling industrial orders. The cooperatives were allowed to sell their products for any prices they could get which did not exceed the high controlled prices for similar wares in government commercial stores. Some taxes were removed from the cooperatives and others were reduced, and the cooperatives were allowed to distribute a portion of their profits among their members. In 1947, the cooperatives and other local, non-govern-

<sup>13</sup> *Russian Economic Notes*, Number 377, pp. 10-12.

<sup>14</sup> *Foreign Commerce Weekly*, April 12, 1941, pp. 75-76.

mental producers were expected to turn out almost 30 million pairs of shoes, almost 40 million pairs of stockings and socks, 54 million meters of cotton cloth, 6 million meters of silk, and 43 million meters of woolen cloth. It was estimated that fulfillment of these goals would increase supplies available to consumers by anywhere from 20 to 60 per cent.<sup>15</sup>

**Private Enterprises** There has even been some place for private enterprises in the socialized economy of Soviet Russia, though all private trading (involving the purchase of goods for resale) is forbidden and private enterprises are excluded from the manufacture of silk goods, cotton goods, leather goods, tobacco products, acids, soaps, cosmetics, paints, and varnishes, and from printing, engraving, and other forms of reproduction. Private individuals, if granted licenses, may operate in bookbinding, boot repairing, cabinet making, carpentry, chimney sweeping, electric fitting, dress making and sewing, house repairing, glazing, hairdressing, laundering, locksmithing, optical work, painting, photography, plumbing, tailoring, and upholstering. Private individuals may make furniture, pottery, cooper's products, musical instruments, and straw articles for sale, and may produce clothing, footwear, leather goods, or articles made of non-ferrous metals, on the basis of orders received, though they may not make them for the market in anticipation of demand. The individual is not allowed to make foods and beverages from purchased materials for purposes of sale, but is permitted to sell such products when made from his own materials. Lawyers, doctors, and dentists may have a practice of their own in addition to their work for the state, stenographers in state enterprises may do private typing for authors and writers, clothing workers may take in private sewing, office cleaners may clean homes and take care of children, and carpenters may build houses for private persons.<sup>16</sup>

**Russian Industrial Results to 1941** We must now examine the Russian claims as to their accomplishments in industrial production under the planned economy in the years from 1928 through 1940. In Table 2, we present statistics of the production of several important industrial commodities in Soviet Russia in the years 1913, 1928, 1932, 1937, and 1940, together with the planned estimates of

<sup>15</sup> Harry Schwartz, *Russia's Postwar Economy*, pp. 43-44.

<sup>16</sup> L. E. Hubbard, *Soviet Trade and Distribution*. London: Macmillan and Company, Ltd., 1938, p. 152.

production for 1932, 1937, and 1942. It is clear that the production of these commodities had been increased very greatly by 1937 and 1940, in comparison with 1913 and 1928, and that even greater accomplishments were planned for 1942. While it would not be fair to evaluate the operation of the Russian planned economy solely on the basis of results in the field of industrial production, there are nevertheless several observations which seem pertinent on the basis of these results.

In the first place, the statistics of industrial production indicate that the Soviet Russian economy, prior to World War II, had made very considerable progress toward one of its planned goals—the industrialization of the economy. Agricultural goods, which had been 57.9 per cent of total national output in 1913, and 45.5 per cent in 1928, declined to 29.3 per cent by 1932 and continued to decline as a percentage of the total thereafter. This meant, of course, that industrial goods increased from 42.1 to 70.7 per cent of total national output over the same period. In 1940, the gross value of all agricultural products was 23 billion rubles while that of all industrial products was 138.5 billion rubles.<sup>17</sup>

Quite apart from their significance as an indication of the industrialization of the economy, the increases in industrial production, if they could be taken at their face value, would cause one to run out of adjectives which are synonymous with "stupendous" and "colossal," for obviously the production of most industrial commodities has not merely increased but has had a manifold increase. One spokesman for Soviet Russia has it that, while industrial production in the capitalist world as a whole increased from 97 to 114 from 1927 to 1937 (on the basis of 1928 = 100), industrial production in Soviet Russia over the same period and on the same base increased from 80 to 583.<sup>18</sup> The great gains of Soviet Russia are partly attributable to rapidly growing industrialization, but full use of fixed productive facilities is another important factor. The same writer points out that, while textile factories in the United States operate 40 hours per week, the Russian textile mills work in three shifts of seven hours, or 126 hours per week. Again, the average American tractor cares for an average of 90 hectares of land per year, whereas the average Russian tractor cares for over

<sup>17</sup> *International Conciliation*, April, 1948, pp. 270-271.

<sup>18</sup> L. Varga, *Two Systems: Socialist Economy and Capitalist Economy*. New York: International Publishers, 1939, p. 40.

500 hectares.<sup>19</sup> From these and other data, he concludes that the Russian utilization of fixed productive facilities is several times that achieved in capitalistic economies. Russian industrial output was only 4.7 per cent of the industrial output of the world in 1928, but it was 11.0 per cent in 1932 and 15.2 per cent in 1937. It was expected to reach 31.0 per cent in 1942.<sup>20</sup>

Finally, the Russian statistics of industrial production are noteworthy in that they suggest the absence of business cycles in the operation of the planned economy. While capitalistic countries were in the throes of a severe depression in 1932 and their industrial outputs were greatly reduced in comparison with 1928, the Russian economy apparently found 1932 a very good year, for the output of most industrial commodities was far above the 1928 level. It is obvious that a country which can avoid business cycles does not have to worry about the cyclical unemployment of its workers. The Russian leaders claim that a planned economy such as their own

<sup>19</sup> *Ibid.*, pp. 56-57.

<sup>20</sup> H. Johnson, *The Soviet Power*. New York: International Publishers, 1940, pp. 92-93.

**TABLE 2**  
**PRODUCTION OF IMPORTANT INDUSTRIAL  
COMMODITIES IN SOVIET RUSSIA**

<i>Item</i>	<i>Units</i>	<i>1913</i>	<i>1928</i>
1 All producers' goods	Billion rubles		8.2
2 Petroleum	Million tons	9.2	11.6
3 Coal	Million tons	29.1	35.4
4 Electric power	Billion kilowatthours	2.0	5.0
5 Pig iron	Million tons	4.2	3.3
6 Steel	Million tons	4.2	4.2
7 Rolled steel	Million tons	3.5	3.4
8 Copper	Thousand tons	31.1	30.0
9 Cement	Million tons	1.4	1.9
10 Sawn lumber and timber	Million cubic meters	11.9	13.6
11 Autos and trucks	Thousands	0.1	0.7
12 Tractors	Thousands		1.3
13 Freight cars	Thousands	11.8	10.6
14 Locomotives	Thousands	0.6	0.5
15 All consumers' goods	Billion rubles		10.1
16. Cotton textiles	Million meters	2227	2742
17 Woolen textiles	Million meters	95.0	93.2
18 Leather shoes	Million pairs	8.3	29.6
19 Sugar	Thousand metric tons	1290	1283
20 Paper	Thousand metric tons	205	284

can always avoid booms and depressions. We shall be in a better position to evaluate this claim after we have examined other phases of the operation of the Russian economic system.

*Russian Statistics.* The Soviet Russian accomplishments in the field of industrial production are, however, open to criticism from several angles. In the first place, there was the question of the reliability of the Russian statistics. The source of data on the Russian economy was the Russian government itself (or various agencies of the government), and this was likely to be a biased source. That is, the Russian government, operating in the midst of a skeptical if not hostile world, was probably anxious to have its accomplishments appear as great as possible and, like some other governments, it may have touched up its statistics a bit at times. Moreover, there was no way to check the statistics adequately and thus to measure and correct any inaccuracies that might exist. Some apologists for Soviet Russia contended that the Russian statistics had to be accurate, since the operation of a planned economy depends to a great extent on having a mass of statistics available, and since the planners would be silly to mislead themselves by concoct-

TABLE 2 (Continued)

IN SELECTED YEARS IN COMPARISON  
WITH PLANNED ESTIMATES

1932 (actual)	1932 (planned)	1937 (actual)	1937 (planned)	1940 (actual)	1942 (planned)
18 0	17 4	55 2	45 5	84 0	114 5
22 3	21 7	30 5	46 8	31 0	54 0
64 7	75 0	128 0	152 5	165 5	243 0
13 0	22 0	36 4	38 0	48 2	75 0
6 2	10 0	14 5	16 0	14 9	22 0
5 9	10 4	17 7	17 0	18 3	28 0
4 2	8 0	13 0	13 0	13 1	21 0
46 7	84 7	97 5	155 0	164 7	215 7
3 5	6 4	5 4	7 5	5 3	11 0
24 4	42 5	33 8	43 0	33 8	45 0
23 9	105 0	200 0	200 0	147 1	400 0
50 6	55 0	80 3	88 5	31 1	
20 2	12 6	59 1	118 0	51 0	120 0
0 8	1 5	1 6	2 8	1 7	2 3
16 3	19 2	40 3	47 2	54 0	
2417	4700	3443	5100	4030	4900
88 7	270 0	105 1	220 0	124 4	177 0
84 7	80 0	164 2	180 0	230 0	258 0
1400	1400	2421	2500	1622	3500
479	900	833	1000		1500

ing unreliable statistics as a basis for making plans and operating the system. However, the need for having reliable statistics for purposes of planning would not have prevented the creation of a separate and unreliable set of statistics for the edification of the outside world.

The various statistics which are stated in terms of rubles were especially open to suspicion, since they were sometimes given in "current rubles" and at other times in "rubles of 1926-1927 value." The Russian leaders saw fit to expand greatly the quantity of money and credit in use and permitted rather considerable increases in prices, so that statistics in terms of current rubles represented the movements of the underlying physical data quite poorly. On the other hand, some industries whose output played a rather important part in the gross value of the output of Russian industry were introduced into the economy only after 1928 and it is difficult to see how the figures for the production of industries which did not exist in 1926-27 could have been calculated in terms of that year's prices.

The production statistics in many cases were likely to reflect the growing output of large-scale government industries only, and an apparent expansion in production meant only that the articles in question were being manufactured to an increasing extent at large factories owned by the government instead of, as formerly, at small enterprises, by craftsmen, or at home. In such cases the increases in official production figures did not represent accurately the changes in the amounts of the goods available for consumption. Finally, data presented by different but supposedly equally authoritative governmental agencies, covering exactly the same economic activities, often varied widely, and attempts were seldom made by these agencies to account for or correct these discrepancies. For these reasons, some writers attempt to analyze and evaluate the operation of the Russian economy without making use of many statistics. Our own inclination is to use the statistics, but with reservations and primarily for the purpose of giving a general impression, both because of the possible unreliability of Russian statistics in general and because our statistics have been obtained from many scattered and uncoordinated sources. However, the statistics for industrial production would still show a remarkable degree of progress over a limited period of time even if they had to be discounted by a very sizable fraction.

*The Quality of Industrial Goods* Our statistics for industrial production are stated, for the most part, in terms of physical quantities of commodities, but the plans for industrial output called for fulfillment in terms of the quality of the goods, the efficiency and productivity of labor, the lowering of costs of production, and the maintenance of satisfactory working conditions and other standards for labor, as well as in terms of physical quantities In practice, the pressure was on the managers of Russian industrial enterprises to achieve fulfillment in terms of physical quantities of goods, and this often resulted in neglect and non-fulfillment in terms of these other matters

Great increases in the quantities of commodities are of little importance unless the commodities are of reasonably good quality, and in this respect Russian industry was notoriously deficient One writer contends that defective goods in some cases amounted to as much as 80 per cent of total output<sup>21</sup> Another says that unsalable products amounted to 37 to 50 per cent of total output in specific industries and up to 80 to 90 per cent for individual trusts and factories<sup>22</sup> The Russian leaders themselves, in their familiar practice of self-criticism, complained bitterly about the wretched quality and variety of manufactured goods, and the Soviet press and the reports of governmental agencies were full of criticisms of the quality of industrial products and excessive spoilage and wastage of materials The problem of quality had apparently not been solved or nearly solved by 1940, for in that year a decree was issued which held managers, chief engineers, and heads of divisions of technical control definitely responsible for the quality of the commodities produced by their enterprises Failure to meet quality specifications was made a crime punishable by 5 to 8 years' imprisonment

*Labor Productivity and Cost of Production* Russian industry also failed to complete the plans with respect to labor efficiency and productivity, and cost of production The First Five-Year Plan aimed at an increase of 110 per cent in labor productivity, but, in announcing the results of the plan, only a 41 per cent increase was claimed One critic contended that even this claim was absurd and

<sup>21</sup> F Utley, *The Dream We Lost* New York The John Day Company, 1940, p 200

<sup>22</sup> B Brutzkus, *Economic Planning in Soviet Russia* London George Routledge and Sons, Ltd 1935, p 205

that the actual net increase in labor productivity was not over 5 per cent.<sup>23</sup> The situation improved greatly under the second plan and, according to one source, labor productivity increased by 82 per cent instead of the planned 63 per cent.<sup>24</sup> However, the increase of labor productivity was still one of the main objectives of the Third Five-Year Plan, and a further increase of 65 per cent was called for.<sup>25</sup> The difficulties experienced with respect to labor productivity and efficiency were indicated by other results of Russian industrial operation. To come even close to plan fulfillment in terms of physical quantities, the number of workers employed in industry had to be increased from 11.3 to 22.8 millions under the First Five-Year Plan, instead of the planned 15.8 millions,<sup>26</sup> and in 1940, with industrial production lagging somewhat, the number of workers in industry had almost reached the planned goal for the end of 1942. While the Russian planners were likely to count such increases beyond the plans in the numbers of industrial workers as evidences of rapid economic progress, they undoubtedly should be considered an indication of low labor productivity in view of the fact that the plans for industrial output were less than completely fulfilled.

The Russian leaders seemed happy to point out that the money wages of Russian industrial workers increased well beyond the planned amounts in each five-year period, but this development, too, is subject to an unfavorable interpretation. That is, one critic has suggested that, because of low labor productivity and the resulting high costs of finished products, the average money wage in industry had to be increased by 150 per cent under the Second Five-Year Plan, instead of by the planned 55 per cent, in order that the workers might be able to take off the market the goods available for their consumption at prices high enough to cover the accounting costs of producing them.<sup>27</sup> Much the same thing seemed to be going on under the Third Five-Year Plan. The original draft of this plan called for a 35 per cent increase in average money wages.<sup>28</sup> Since the average wage in industry was 2772 rubles in 1937, this would have meant an average wage of 3742 rubles by 1942. Actually, the

<sup>23</sup> *Ibid.*, p. 207.

<sup>24</sup> Alexander Baykov, *The Development of the Soviet Economic System*, p. 286.

<sup>25</sup> *Ibid.*, p. 290.

<sup>26</sup> F. Utley, *op. cit.*, p. 201.

<sup>27</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, p. 163.

<sup>28</sup> *Russian Economic Notes*, Number 6, p. 6.

average money wage in industry had risen to 4069 rubles by 1940, and promised to be much higher by the end of 1942.<sup>29</sup> Since the prices of finished products are based in part on arbitrary accounting costs for land and capital goods, the low labor productivity could have been offset in part by reducing the charges for the other productive factors, but apparently productivity was too low to permit this device to be very effective.

In comparing the productivity of Russian workers with that of workers of other countries, Brutzkus has pointed out that, toward the end of the First Five-Year Plan, the output of coal in the Donetz region of Russia was 0.61 ton per worker shift, as compared with 1.53 tons in the German Ruhr, 1.2 tons in England, and 4.85 tons in the United States. Pig iron produced per worker per month in Russia averaged 24 tons, as compared with 140 tons in the United States, and steel production per worker per month was 17 tons in Russia and 47 tons in Germany.<sup>30</sup> Even toward the end of the Second Five-Year Plan, high Russian officials admitted that the productivity of the average Russian worker, operating with comparable equipment, was only one-fourth to one-half that of the average American worker. Other estimates have been even less favorable to the Russian worker. With Russian industrial managers under great pressure to complete the plans in terms of physical quantities of goods, the low productivity of Russian labor is supposed to have led to widespread violations of labor standards with regard to hours of work, rest days, and other matters, as provided by the Labor Code and the economic plans.<sup>31</sup> We shall look into this matter in some detail in connection with our analysis of the status of labor in Russia in Chapter 17.

*Depreciation and Replacement.* The results of planned industrial operation in terms of physical quantities of goods produced do not show what has happened to plant, machinery, and equipment in achieving the stated results. Obviously, increasing outputs of physical commodities need to be discounted somewhat if they have been obtained at the cost of an abnormal increase in the wearing out and breaking down of machinery and equipment, and the same is true of increases in the productive facilities of industries if adequate

<sup>29</sup> N. Vosnesensky, *Economic Results of the USSR in 1940 and the Plan of National Economic Development for 1941*. Moscow: Foreign Language Publishing House, 1941, pp. 10, 32.

<sup>30</sup> B. Brutzkus, *Economic Planning in Soviet Russia*, p. 207.

<sup>31</sup> See, for example, F. Ulley, *The Dream We Lost*, pp. 175-176.

provision has not been made for the maintenance and repair of old productive facilities. If adequate account of the costs of maintenance, repair, and replacement of machinery and equipment is not kept in computing the costs of finished commodities, a further element of unreliability is introduced into Russian claims as to the results of industrial operation.

It was frequently said that Soviet Russian planners and industrial officials were very lax in regard to these matters. According to a Russian source:

In the plan of capital construction for former years, the amount of expenditure for capital repairs was excessively reduced, provision was not made for the necessary renewal of worn out parts, and there was a disparity between the expenditure on current and capital repairs. Capital repairs were "planned" in such a way that repairs were only undertaken when the equipment was worn out. The funds allocated for capital repairs were clearly inadequate. The amount of amortization devoted to capital repairs in previous years was obviously insufficient and did not provide for proper renewal of plant. According to the fulfillment figures of 1937, the wear and tear of industrial plant controlled by the National Commissariat of Heavy Industry represented 21.7 per cent of the original cost of the plant.<sup>32</sup>

*The Efficiency of Management.* It is clear that the blame for any shortcomings in the field of industrial operations in Soviet Russia cannot be placed entirely on the shoulders of the ordinary workers in industry. Some of the faults can be traced in part to the economic planners themselves, while others were due to the ineffectiveness of industrial management. In connection with management, the problem was at least in part to discover and provide some force making for business efficiency comparable to that furnished under capitalism by the competition of private interests. At one time the planners furnished raw materials, building materials, machinery, and equipment to industry at prices below the level of accounting costs as an incentive to management, making up the deficit from budgetary funds. Later, an attempt was made to place each industry on a self-supporting basis. This involved fixing the prices of finished products at the level of average cost in the various industries, so that the gains of some enterprises would make up for the losses of others. Since 1936, the problem of making each enterprise self-sufficient has been under attack. In that year, a "director's fund" was set up for each firm. It was planned to put 4 per cent of planned profits

<sup>32</sup> *Planovoe Khozyaistvo*, 1938, Number 5, p. 52, and Number 10, pp. 52-54.

and 50 per cent of unplanned profits into this fund, which could then be used for improved housing, bonuses, cultural activities, and technological improvements. Again the purpose was to provide incentives to efficiency, but the director's fund could not mean much to those unfortunate enterprises which could not possibly make ends meet.

The Russian planned industrial system seemed to suffer continuously from a shortage of trained managers. In the early days of the Soviet regime, numerous managers, engineers, and other experts were imported from other countries because there were comparatively few qualified people of these types left over in Russia after the revolution. Nevertheless, in 1929, 43.7 per cent of the positions in industry requiring higher technical training and 59.7 per cent of the positions requiring secondary technical training were filled by people without any special technical qualifications, that is, by people with some practical experience but without any special theoretical instruction.<sup>23</sup> In later times, Russian managers were selected from persons specially trained for the work. In many cases they were former workers who had shown more understanding and initiative than the rank and file of their fellows. In 1938, about half of all factory directors and trust managers in the important Ministry of Heavy Industry were individuals under 35 years of age.<sup>24</sup> Also indicative of the shortage of managers were reports that some managers, who had been condemned to execution or long terms of imprisonment for inefficiency and "wrecking," only disappeared for a month or two and then came back into circulation again as managers of other plants in other parts of the country.  
*Over- and Under-Fulfillment of Plans* According to Russian authorities, the First Five-Year Plan as a whole was fulfilled to the extent of 93.7 per cent, while the Second Five-Year Plan was completely fulfilled.<sup>25</sup> However, these estimates were based on the values of products in terms of rubles, rather than on physical quantities of products, and it is clear that fulfillment in terms of rubles may be increased by rises in the prices of products as well as by increases in their physical output. If we attempted to compute simple averages for plan fulfillment in terms of physical quantities of commodities on the basis of the statistics presented in Table 2,

<sup>23</sup> Alexander Baykov, *The Development of the Soviet Economic System*, p. 161.

<sup>24</sup> *Moscow News*, January 2, 1939.

<sup>25</sup> Alexander Baykov *op. cit.*, pp. 168, 282.

the best we could get would be around 70 per cent fulfillment for the First Five-Year Plan and 80 per cent for the Second Five-Year Plan. Of course, the results for the various individual commodities should be weighted in some way, and many more commodities should be included in the average, in order to obtain an accurate index of plan fulfillment. However, no reasonable system of weighting would produce fulfillment averages of anything like 93.7 or 100 per cent and, while our data deal with only a few commodities, these commodities are probably not the ones for which productive results were least favorable, since the Russian authorities have seen fit to give out more complete data for these goods than for others.

We must also remember that any index of plan fulfillment is of necessity an average, and there is serious doubt as to the significance of the average in this case. That is, it is questionable whether we should allow over-fulfillment in one part of the plan to cancel under-fulfillment in some other section, as the process of averaging obviously does. A fulfillment figure of 150 per cent for automobile chassis and one of 50 per cent for automobile tires would produce an average fulfillment of 100 per cent, and also many a headache for the planners and the prospective users of the commodities in question. In spite of a high average level of fulfillment, great under-fulfillment in important individual fields led to delays in the development of more progressive branches of industry, the manufacture of incompletely finished articles, changes in standards, and the incomplete utilization of productive facilities elsewhere in the economy.

Many factors operated to produce over-fulfillment and under-fulfillment of the Russian economic plans. Good and bad weather conditions in particular years affected the size of crops, the quantities of food available for consumers, the quantities of raw materials at the disposal of industries, and the quantities of goods available for export. Other disruptions resulted from the failure to attract foreign capital to certain Russian industries as expected, and depressed conditions in foreign markets which limited Russian exports or decreased the purchasing power of these exports in terms of the industrial goods which the planners hoped to import. Military emergencies diverted productive resources from their planned uses. In some cases, the planners changed their policies during the course of a plan, with very serious results from the point of view of plan fulfillment. For example, the First Five-Year Plan called for

an increase in the quantity of land under socialized cultivation so that at the end of the plan some 17.5 per cent of the total cultivated area would be in the hands of state or collective farms, as compared with 2.7 per cent at the beginning of the plan. Actually, because of a change in policy, about 78 per cent of the cultivated area was socialized within the five-year period.<sup>26</sup> This result brought great pressure to bear on the industries producing farm machinery, and disrupted the plans for investment, transportation, the production of coal and ores, and the distribution of the skilled labor supply. In fact, some of the greatest productive establishments created in this period were not even contemplated in the original draft of the First Five-Year Plan.

Finally, over- and under-fulfillment resulted from sheer human inability to make accurate estimates in advance as to the results which could be obtained from the use of given quantities of labor and other resources. As a result, we found 51.4 per cent fulfillment in the production of cotton textiles, 57.4 per cent for sawn lumber and timber, 100.2 per cent for sugar, and 160.3 per cent for freight cars.<sup>27</sup> Incidentally, some of the fulfillment figures were very difficult to reconcile with each other. It was not easy to see, for example, how machine building could have fulfilled the first plan to the extent of 181.2 per cent, when iron ore production, pig-iron production, and steel production reached only 62.9, 62.0, and 56.7 per cent, respectively, unless some other lines of production using iron and steel were choked off almost completely.<sup>28</sup>

*Capital Goods and Consumers' Goods.* Our statistics for Russian industrial production also indicate that much greater success has been enjoyed in the production of capital goods than in the production of consumers' goods. Bare plan fulfillment for each category of goods would have resulted in an amazingly great emphasis on the production of capital goods, for the First and Second Five-Year Plans called for the production of about as many capital goods as consumers' goods, while the Third Five-Year Plan called for the production of 114.5 billion rubles worth of producers' goods in 1942 as compared with 69.5 billion rubles' worth of consumers' goods. Actually, the output of producers' goods in 1932 reached 103.4 per cent of the planned estimate, while that of consumers'

<sup>26</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, pp. 159-160.

<sup>27</sup> These percentages were computed from the data presented in Table 2.

<sup>28</sup> M. T. Florinsky, *op. cit.*, p. 162.

goods reached only 84.9 per cent At the end of the Second Five-Year plan, the output of producers' goods was 121.3 per cent of the planned estimate, while that of consumers' goods was only 85.4 per cent of the planned estimate<sup>20</sup> The planned results were favorable from the point of view of the rapid industrialization of the economy, and the actual results were even more favorable, but there is no doubt that they had serious effects on the standards of living and general economic welfare of the people The planners decided that rapid industrialization, rather than large immediate increases in consumers' goods, was what the people needed, and there is little evidence that the wishes of the people in this matter were ever really consulted

*Russian Industrial Capacity* Even if we concede all the Russian claims with regard to the results of planned industrial operation, the fact still remains that Russia, in proportion to her area, population, and resources, was far from being an advanced industrial country by 1940 In Table 3, we compare Russian industrial capacities in several important lines with those of the United States in 1940, and note that Russian productive facilities were sometimes large fractions of United States productive facilities and sometimes small fractions, but they were always fractions Clearly, Russia had a long way to go in her self-appointed task of outstripping the leading capitalistic countries in industrial production

*Conclusion as to Prewar Results* It should not be imagined that we have been inventing criticisms of the results of planned industrial operation in Russia or that we have been listening only to critics who are unfavorably disposed toward the Soviet system, for most of our criticisms were stated and repeated many times over in the Russian press and in the speeches and writings of Russian leaders busily engaged in their practice of enthusiastic self-criticism Certainly it is necessary to conclude that, as of 1940, Russian economic planning was still in the experimental stage and had much still to gain in matters of precision and definiteness It was not safe to decide that Russia had found as yet the best possible solutions to the problems of industrial production On the other hand, the criticisms which have been directed at the results of planned industrial operation in Russia should be considered only to qualify, and not to deny, the undoubtedly accomplishments and progress which were achieved

<sup>20</sup> These percentages were computed from the data presented in Table 2

TABLE 3

INDUSTRIAL PRODUCTIVE FACILITIES OF SOVIET RUSSIA  
AND THE UNITED STATES

Item	Unit	Reported Russian Productive Facilities in 1940	United States Productive Facilities in 1940
1 Electric power capacity	Millions of kilowatts	81 <sup>c</sup>	42 0
2 Oil wells in operation	Thousands	96 <sup>a</sup>	401 2
3 Oil refinery capacity	Million tons	33 7 <sup>b</sup>	210 3
4 Cracking-plant capacity	Million tons	6 9 <sup>b</sup>	45 9
5 Blast furnaces	Number	122 <sup>b</sup>	231
6 Pig-iron capacity	Million tons	15 7	49 9
7 Steel furnaces	Number	348 <sup>b</sup>	1,200
8 Steel capacity	Million tons	19 9	72 6
9 Locomotives on hand	Thousands	24 9	45 2
10 Freight cars on hand	Thousands	809 6	1,680 5
11 Railroad lines	Thousand kilometers	102 5	618 9
12 Trucks on hand	Thousands	767 8 <sup>a</sup>	4,497 6
13 Automobiles on hand	Thousands	157 2 <sup>a</sup>	26,915 8
14 Telephone and telegraph lines	Million kilometers	1 6	147 6 <sup>a</sup>
15 Cement capacity	Million tons	8 2	43 7
16 Sawmill capacity	Million cubic meters	31 5 <sup>a</sup>	85 0

<sup>a</sup> 1939 figure<sup>b</sup> 1938 figure<sup>c</sup> 1937 figureSOURCE *Fortune*, July, 1941, p. 87

**Early Wartime Losses** After the beginning of the war with Germany, the Russians gave ground rather rapidly before the invaders. From June, 1941, to the end of 1942, the part of Russia conquered by Germany was as large as the eastern and southern portions of the United States, including Texas. The area contained half of Russia's working coal mines and 87 per cent of her railroad mileage. It had formerly produced two-thirds of Russia's iron ore, 60 per cent of the pig iron, half of the steel, 25 per cent of the machines, and half of the electric power.<sup>40</sup> Other wartime productive losses, as percentages of 1940 output, were oil 16, steel 55, rolled steel 61, cement 52, timber 36, sawmill products 55, and paper 40. Half her railroad locomotives and 47 per cent of the freight cars were also lost.<sup>41</sup> Many people outside of Russia felt that these losses would soon prove crippling.

<sup>40</sup> L. Snow, *People on Our Side* New York: Random House, 1944, pp. 69, 70, and M. Dobb, *Soviet Planning and Labor in Peace and War* New York: International Publishers, 1948, pp. 101, 102.

<sup>41</sup> *International Conciliation*, April, 1948, p. 264.

**Production Successes** But in spite of the losses just listed, Russia's war production on the whole was not only maintained but also increased. According to one estimate, Soviet heavy industry produced 14 per cent more goods in 1945 than in 1940, but the production of goods for civilian consumption was at only a little more than half the 1940 level.<sup>42</sup> The secret of Russia's success in war production was the rapid development of the Ural, Siberian, and Central Asian regions. The machines and equipment of many factories, including 1300 large industrial plants, were "leapfrogged" from western Russia to these new regions. In preparation for such a development, machines had been lightly anchored in place and numbered for reassembling. They were loaded on cars, sometimes hundreds of cars to a factory, and moved hundreds or thousands of miles. Altogether more than a million carloads of machines, equipment, and materials were moved eastward in the summer and fall of 1941.<sup>43</sup> In the new regions, sites had been cleared in readiness or were rapidly cleared. Some factory buildings had already been constructed, and others were soon erected. Sometimes large numbers of workers were moved, along with the machinery and equipment, and were housed in hastily constructed barracks.

The Russians had large stock piles of foods and essential materials and were also able to rely on local materials in the new regions to a considerable extent. The Ural region, for example, contains all but four of the known chemical elements.<sup>44</sup> Reliance was also placed on intensification of the workers' efforts, curtailed replacements of machinery in nonessential fields of production, standardization of products, improvisation, and training on the job. Women and young people of both sexes were brought into employment, given rapid training, and stimulated by honors and socialist competition. Housewives were changed into factory workers in two weeks' time. Technical training programs were rapidly extended and eventually included about half of all students beyond the seventh grade.

In comparison with what most people expected, Russian war production was truly prodigious. Indeed, Russia conducted the war against Germany almost entirely on her own power in 1941 and 1942. From the beginning of the war through the siege of

<sup>42</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 10.

<sup>43</sup> *Ibid.*, p. 9.

<sup>44</sup> E. Snow, *People on Our Side*, p. 147.

Stalingrad, Russia received only about a billion dollars' worth of aid from the United States and Britain, and such an amount of munitions and supplies did not go far in World War II. On the other hand, Russia required large amounts of material assistance from her Allies in order to drive the enemy out of the country and back to the heart of Germany.

*The Problem of Rehabilitation* Under the circumstances prevailing at the time, it was not surprising that Russia failed to adopt a new Five-Year Plan in 1943, but instead embarked on a course of rehabilitating the devastated areas of the country as fast as they were reconquered. Some 1710 towns and cities, 70,000 villages, and 6 million buildings had been partly or completely destroyed, and 25 million people had been made homeless. About 32,000 factories and plants, 217,000 shops and stores, and 65,000 kilometers of railroad track had been ruined, while 15,800 locomotives and 500,000 freight cars had been destroyed. The direct cost of the war was estimated at 128 billion dollars and the total cost, direct and indirect, at 357 billion dollars.<sup>45</sup>

*The Fourth Five-Year Plan* Although the work of rehabilitation was only moderately well under way, the Russian leaders were ready to embark on a Fourth Five-Year Plan by April, 1946, about a year after the end of the war with Germany. Like its predecessors, the new plan is rather ambitious. By 1950, the gross product of industry is to be increased to 205 billion rubles (as compared with 138 billions in 1940), and the production of food and other consumers' goods is to increase by 17 per cent a year over the period. Agricultural production in 1950 is to be 27 per cent above that of 1940. New capital investments are to amount to 250.3 billion rubles over the five years. National income will increase, according to the Plan, to 177 billion rubles in 1950, as compared with 125.5 billions in 1940.

Employment in the national economy (government owned and operated) in 1950 is to reach 33.5 million workers, an increase of 6.25 millions in five years. Wages on the average are to increase to 500 rubles per month. Labor productivity is to increase by 36 per cent over the prewar level, and 70 per cent of the general growth of industrial production is to depend on this factor. Expenditures on education and culture will increase to 106 billion rubles over

<sup>45</sup> *International Labor Review*, January February, 1946, p. 71, and *Soviet Russia Today*, May, 1948, p. 15.

the period, or  $2\frac{1}{4}$  times the prewar expenditures, technical schools will be expanded to accommodate 12 million students; and some 42.3 billion rubles will be spent for the construction of 72.4 million square meters of new housing (as compared with 15.5 billion rubles and 30 million square meters under the third plan). Small hydro electric stations with an aggregate capacity of one million kilowatts will be constructed for rural electrification, over three million acres of land will be reclaimed by irrigation or drainage, and over 40 billion rubles will go into the restoration and development of railroad transportation.<sup>46</sup>

In Table 4 we present statistics for the actual production of a number of important industrial commodities in 1940, 1945, and 1947 in comparison with planned estimates for 1942 and 1950. It will be noted that the outputs planned for 1950 are uniformly above those actually achieved in 1940, though sometimes not by very much, but that several outputs planned for 1950 are well below those previously planned for 1942. The 1950 outputs, if

TABLE 4

*PRODUCTION OF IMPORTANT INDUSTRIAL COMMODITIES IN  
SOVIET RUSSIA IN 1940, 1945, AND 1947 IN COMPARISON  
WITH PLANNED ESTIMATES FOR 1942 AND 1950*

Item	Units	1940 (actual)	1942 (planned)	1945 (actual)	1947 (actual)	1950 (planned)
1 All producers' goods	Billion rubles	84.0	114.5	96.0		137.0
2 Petroleum	Million tons	31.0	54.0	18.4	24.5	35.4
3 Coal	Million tons	165.5	243.0	136.0	168.0	250.0
4 Electric power	kilowatthours	48.2	75.0	40.0		82.0
5 Pig iron	Million tons	14.9	22.0	9.1	11.6	19.5
6 Steel	Million tons	18.3	28.0	13.4	16.6	25.4
7 Rolled steel	Million tons	13.1	21.0	8.6	12.4	17.8
8 Sawn lumber and timber	Million cubic meters	33.8	45.0	31.8	39.5	39.0
9 Tractors	Thousands	31.1		7.6	27.4	112.0
10 Autos and trucks	Thousands	147.1	400.0			500.0
11 Locomotives	Thousands	1.7	2.3			4.0
12 All consumers' goods	Billion rubles	54.0	69.5	31.0		68.0
13 Cotton textiles	Million meters	4030	4900	1616	2514	4686
14 Woolen textiles	Million meters	124.4	177.0	57.0	98.4	159.4
15 Leather shoes	Million pairs	230.0	258.0	60.0	107.5	240.0
16 Hosiery	Million pairs	480.0		83.0	184.2	580.0

<sup>46</sup> Soviet Russia Today, May, 1946, pp. 32, 33 and December, 1946, pp. 9, 10.

achieved, will represent very large increases over those of 1915. The emphasis will still be on producers' goods rather than consumers' goods in 1950, with 137 billion rubles' worth of the former and only 68 of the latter being produced, according to plan. To reach these goals, however, consumers' goods will have to show an increase in output of 119 per cent over 1945, while only a 43 per cent increase will be required for producers' goods.

*Productive Results in 1946 and 1947.* In 1946, the first year of the Fourth Five-Year Plan, only moderate increases in industrial production were achieved. Total civilian production is reported to have increased by 20 per cent over 1945, which is a relatively modest showing if we remember that Soviet industry had been very largely occupied with war production during at least the first half of 1945.<sup>47</sup> One obstacle to the complex task of reconversion was the clumsiness and bureaucracy of the industrial organization. Loss of time and output resulted from the poor coordination of various plants and Ministries, and there were cases in which some plants stood idle for lack of machines or materials which other plants had available and could not use.

Soviet industry was also hampered in 1946 by a shortage of workers, especially skilled workers. Many of the workers employed were new recruits to industrial production and they had to work with machinery and equipment which were in poor condition because of excessive use and inadequate maintenance during the war. The rate of labor turnover was excessively high, and labor discipline was poor. Another factor in the situation was a high level of waste, spoilage of materials, and rejected products. Finally, the construction of new plants and the rebuilding of old ones lagged considerably behind the plans. This was partly the result of shortages of building materials and labor and partly due to confusion, inefficiency of management, and defective planning in the construction industry.<sup>48</sup> In spite of all obstacles, however, it was reported that 13 out of 28 Ministries had fulfilled or exceeded plans for the year.<sup>49</sup>

The situation in industrial production in 1947 was much more satisfactory. Gross output increased by 22 per cent over 1946, 21 out of 28 All-Union Ministries announced over-fulfillment of the

<sup>47</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 21.

<sup>48</sup> *Ibid.*, pp. 25-27.

<sup>49</sup> *Soviet Russia Today*, November, 1947, p. 50.

annual plans, and industrial production reached the 1940 level in the fourth quarter of the year<sup>50</sup> Nevertheless, outputs of 18 out of 31 individual commodities lagged behind the plans, and there were many important commodities for which no reports were available. Some of the reported percentages of fulfillment were down in the lower 70's Housing construction was a particularly soft spot, with only about 15 million square meters constructed in 1946 and 1947 together, or about the amount needed each year to fulfill the Five Year Plan<sup>51</sup> On the whole, it was clear that the production of many industrial commodities had a long way to go in a hurry if plans for 1950 were to be fulfilled. However, whether or not the Fourth Five-Year Plan for industry is fulfilled, the Russians are at least entitled to an "E for effort"

#### QUESTIONS

- 1 "The organization of production under capitalism is left to private individuals for the most part" Explain
- 2 How and why do the governments of capitalistic countries sometimes attempt to influence the productive results achieved by their economies?
- 3 "Production under socialism would make use of many methods and organizational forms which characterize capitalistic production" Show whether you agree
- 4 "Under socialism, all types of production would be controlled and operated exclusively by governmental enterprises" Do you agree? Explain
- 5 How would the government of a socialistic economy control any private or cooperative enterprises and industries which it permitted to exist?
- 6 "Modern socialism would be undesirable because it would involve the ownership and operation of all lines of economic activity by our federal government in Washington" Discuss
- 7 Indicate the relationships between trusts, commissariats, administrations, and plants in Soviet Russian industry prior to 1939 and point out the functions of each of these organizations
- 8 How was the organization of Soviet Russian industrial production changed after 1939? Explain
- 9 "The position of plant managers in the Russian industrial organization is not a very attractive one" Explain
- 10 "The ownership and operation of industry by various governmental

<sup>50</sup> *Soviet Russia Today*, June, 1948, p. 30

<sup>51</sup> *International Conciliation*, April, 1948, pp. 275-278

units in Soviet Russia correspond rather closely to the prospectus given out by modern socialists" Show whether you agree

- 11 What has been the importance of cooperative and private enterprises in Soviet Russian production?
- 12 "According to official Russian statistics, the results of planned industrial production through 1910 were amazingly good" Explain
- 13 "There are several reasons for questioning the reliability of Soviet Russian statistics on industrial production" Explain
- 14 What are the principal criticisms that may be directed at the results of planned industrial production in Soviet Russia through 1910?
- 15 "Statistics on the physical volume of production do not mean very much unless we know something about such matters as labor productivity, cost of production, the quality of the goods, and the depreciation of plant and equipment" Explain
- 16 "The under-fulfillment and over-fulfillment of various phases of the plans for industrial production may cancel each other in terms of mathematical averages but not in their effects on the economy" Show whether you agree
- 17 "The planned production of capital goods in Soviet Russia was much more successful than that of consumers' goods through 1940" Explain
- 18 How would you criticize the claim of Soviet Russian leaders that a given Five-Year Plan had been fulfilled to the extent of 93.7 per cent?
- 19 "In view of the grave economic losses that were suffered, industrial production was remarkably well maintained in Soviet Russia during World War II" Do you agree? Explain
- 20 How was Soviet Russia able to keep industrial production going during World War II?
- 21 Describe and evaluate the goals of Soviet Russia's Fourth Five Year Plan
- 22 "Industrial production in Soviet Russia increased only moderately during 1946" Why?
- 23 "Industrial production in Soviet Russia in 1947 was so satisfactory that the fulfillment of the Fourth Five-Year Plan in this field seemed certain" Show whether you agree

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## CHAPTER 8

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### **THE ORGANIZATION OF PRODUCTION**

*(Continued)*

#### *The Organization of Production in Britain under Partial Socialism*

***The Organization of Nationalized Industries*** Discussion of the organization of production in Britain under partial socialism must deal with two subjects—the nationalized industries and the rest of the economy Among the former industries, the coal industry is operated by a single publicly owned and publicly financed agency, the nine-man National Coal Board appointed by the Minister of Fuel and Power The Board is, of course, ultimately responsible to the Minister, who is in turn responsible to Parliament The Minister is empowered to give the Board directions of a general character with regard to matters of high policy which affect the national interest, and must approve the Board's plans for major capital expenditures and for education, training, and research He has full powers of investigation and securing necessary information, and will appoint auditors for the Board's accounts, review the accounts, and lay them before Parliament Under the National Coal Board, the detailed operation of the mines is delegated to a number of Regional Coal Boards

In the case of the Bank of England, the entire capital stock of the Bank was transferred to a nominee of the Treasury, so the Bank continues to operate as a corporation under public ownership The appointment of the Court of Directors, consisting of the Governor, Deputy Governor, and 16 Directors, has become the prerogative of the King, acting on the advice of his Government



nated, and economical system of electricity supply for all parts of Great Britain except the area covered by the North of Scotland Hydro-Electric Board. There are 14 Area Boards which supply electricity to the consumers within their regions. The Central Authority will coordinate the policies of the Area Boards and exercise a considerable amount of financial control over them. There will be a consultative Council within each area to represent the interests of consumers, organizations, and persons interested in the development of electricity services within the area.

In general then, the lines of authority in connection with the nationalized industries seem to run from the Parliament through the Cabinet, individual Ministers, and central agencies of some kind, down to lower agencies which actually manage the industries and plants and are assisted by various advisory boards and councils. Naturally, in such an organization, much concern is felt over the prospective efficiency of the nationalized industries. The Labor Government is confident that efficiency will be attained. The accounts of public industries are to be kept in the same fashion as those of private industries and will be subjected to careful scrutiny. It is hoped that a true picture of costs will be obtained, whether or not these costs will be covered by receipts from operations. The government is also counting on better relations with labor as a force making for efficiency. Workers will be free to strike, and collective bargaining will continue as before, but, since nationalization of key industries has been a trade union objective for many years, it is hoped that the workers will be imbued with a determination to make it succeed. Whether these hopes will be realized in practice remains to be seen.

*Governmental Control of Private Industries.* Apart from these nationalized industries, economic activity in Britain is supposed to be organized and operated in the usual capitalistic fashion but within the framework of the general plans set up by the Cabinet and the Economic Planning Board. Businesses are to be free to organize in any of the traditional forms, they may be small, medium, or large in size, and may make their decisions on the usual capitalistic bases. However, the actual situation is quite different, and private industries and businesses are subject to detailed governmental regulations and controls in practically all their activities.

The government has wide powers to encourage the development

of a variety of industries in areas which have sometimes been depressed in the past because they were dependent on single industries Through the Ministry of Town and County Planning, it frames and executes a national policy for the use of land, including its distribution among industrial, agricultural, residential, and recreational uses It has control over industrial, residential, and public construction, and can turn on or shut off construction at will, either as a whole or in particular branches Permits are required for building, for all repairs over a very low limit, and for the purchase of building materials The Ministry of Works has the task of coordinating all building plans to insure that the supply of building materials is adequate and that the right priorities are maintained

The government controls the kinds and quantities of goods to be produced by industry, though by indirect rather than direct methods It has control over credit and investment policy and over all new access to the capital market, being able to establish priorities that it deems essential to the national interest It allocates and rations materials and supplies among industries and businesses It can keep people from accepting jobs in nonessential fields, furnish them with opportunities for employment in essential industries, and even direct them into jobs in the latter areas By furnishing or withholding credit, capital goods, materials and supplies, and labor, the government is able to control the kinds and quantities of goods which firms and industries will produce, and even induce them to agree to produce desired amounts of "utility goods" (goods of standard design but adequate quality, designed to meet essential needs, and sold at low, fixed prices, without purchase tax) As a last resort the government can even replace the inefficient managers of firms and industries with governmental nominees

The government controls the uses and prices of foreign exchange, requiring the recipients of foreign exchange and specified currencies to sell them to the Exchange Control The import or export of sterling currency is forbidden, except under rare conditions The government has extensive control over imports and exports Many imports, especially basic foods and raw materials, are bulk-purchased abroad solely by governmental representatives Other items are imported by private firms under a system of import licenses Exports are also controlled by a licensing system A target for total exports is set up by the government, and explicit targets for each

industry and each section of each industry are established. Control of the exports of individual firms and the direction of their exports to specific destinations are accomplished by the manipulation of building, equipment, and raw material licenses, and supplies of labor, rather than by direct orders.

The government regulates the crops which farmers may grow and the productive methods they may employ. It monopolizes the purchase of most home-grown food supplies. For "bad husbandry," it can evict tenant farmers and order owner-occupiers to quit their farms and turn them over to persons approved by the Minister of Agriculture. It can even require farm owners to sell their farms to the government if the Minister is satisfied that the farms are not being satisfactorily managed. The government controls the prices of a considerable number of economic goods, and rations many scarce consumers' goods and services among the citizens. Under all these conditions, it is small wonder that, when the Deputy Prime Minister told a press conference in August, 1917, that England is still a free country, the proceedings were interrupted for two minutes by laughter.<sup>1</sup>

*Recent Results in Industrial Production.* Leaving other aspects of the economy for discussion in later chapters, we may close the present section with a few comments on industrial production in Britain in 1917 and the targets for industrial production in 1918. On the whole industrial production increased considerably in 1917 and toward the end of the year was well above the 1913 or prewar level in many lines. In late 1917, the output of electricity was running about 71 per cent above the 1913 level. Comparable percentages were 45 for rayon and nylon yarn, 30 for sulphuric acid, 105 for superphosphate, 40 for freight cars, 425 for agricultural tractors, 63 for motor trucks, 91 for merchant shipbuilding and 27 for cement. Over the whole year, steel production was about 35 per cent greater than in 1913.<sup>2</sup>

However, there were some soft spots in the British industrial situation in 1917. The coal industry, bell-wether of the British industrial flock, produced about 13 per cent less in 1917 than in 1913, in spite of some increase in its labor force and output per worker and some decrease in absenteeism. Late in 1917, automobile

<sup>1</sup> *The Chicago Tribune*, September 8, 1917.

<sup>2</sup> *Statistical Bureau's Post-war New York Branch Information Service*, "pp. 7-16."

production was running about 8 per cent below the 1938 level Comparable percentages were 37 for cotton yarn, 46 for cotton cloth, 17 for worsted yarn, 30 for building bricks, and 58 for roofing slate<sup>3</sup> And, of course, industrial production as a whole was not nearly sufficient to satisfy the demands of British consumers and provide the volume of exports which was necessary if the country's trade were to be brought in balance

The targets for industrial production which were set up for 1948 provided in general for reasonable increases in output over 1947 Coal production was to increase from 197 to 211 million tons In coal mining machinery, 1400 coal cutters were to be produced instead of 1172, some 250 power loaders instead of 109, and 4700 conveyors instead of 2666 Steel output was to increase from 127 to 14 million tons, cotton yarn output from 740 to 900 million pounds, worsted yarn from 154 to 190 million pounds, woolen and worsted cloth from 233 to 290 million yards, rayon (continuous filament) from 119 to 150 million pounds, rayon (staple fiber) from 82 to 105 million pounds, and tankers completed from 120 to 175 thousand gross tons<sup>4</sup> Nevertheless, the leaders of the Labor Government regarded 1948 as a year of transition, with the problems of industrial production far from completely solved

### *The Organization of Production under Fascism*

*The Formation of Category Corporations in Italy* Italy and Germany, in operating their fascist economic systems, had to devise ways and means of achieving rather complete governmental control over production in spite of the fact that the productive enterprises in their economies remained, for the most part, privately owned and operated It was not until 1934 that the fascist organizations for controlling production were established in Italy, though the legal basis for them had been provided in 1926 In 1934, 22 so-called category corporations were established by decree The category corporations were divided into three broad groups "I Corporations representing branches of economic activity which involve agricultural, industrial and commercial operations II Corporations representing economic activities involving industrial and commercial operations only III

<sup>3</sup> *Ibid.*, pp 7-16

<sup>4</sup> *Economic Survey for 1948* London His Majesty's Stationery Office, 1948, pp 86, 87

Corporations representing enterprises established for the performance of services "<sup>5</sup> The first of these groups included originally eight corporations, namely those of grains, vegetable, flower and fruit growing, viticulture and wine production, edible oils, sugar beets and sugar, animal husbandry and fishing, wood and wood products, and textile products In the second group were the corporations of building and construction, metallurgy and machinery, clothing industry, glass and ceramics, chemical industries, paper and printing, extractive industries, and water, gas, and electricity The service group contained the corporations of professions and arts, internal communications, sea and air transportation, tourist and hotel trade, credit and insurance, and theater and public entertainment <sup>6</sup>

These category corporations were reorganized to a slight extent in 1938 By a process of consolidation, the number of corporations in the first group was reduced from eight to six (cereals, horticulture, wines and edible oils, animal husbandry and fishing, wood and wood products, and textile products) The number of corporations in the second group was increased from eight to ten by setting up separate corporations for metallurgy and machinery (which were formerly covered by a single corporation) and by splitting the corporation for extractive industries into corporations for (1) liquid fuels and (2) mining and quarrying The corporations in the third group were left unchanged Thus the category corporations, like the Russian Ministries, seemed to be set up on an experimental basis and were subject to occasional revision

*The Nature of the Category Corporations* It should be emphasized that the establishment of the category corporations did not mean a fundamental reorganization of Italian production The category corporations were merely governmental control agencies superimposed upon the old organization of production, which operated as before on the basis of single enterprises, partnerships, corporations, cartels, and combinations The category corporations, unlike ordinary corporations, were not business enterprises, and they did not produce any commodities or services They did not own and operate the underlying enterprises, and their control over these enterprises developed only gradually through time Thus, to con-

<sup>5</sup> W G Weil, *Fascist Economic Policy*, p 108 Reprinted by permission of the President and Fellows of Harvard College

<sup>6</sup> *Ibid*, pp 109 116

sider a single example, the category corporation of the clothing industry consisted of "a president and 49 members, including representatives of the Fascist Party (3), Clothing Industry (3 employers', 3 workers'), Fur Industry (1 employers', 1 workers'), Hat Manufacture (1 employers', 1 workers'), Boot and Shoe and Leather-Novelty Industry (2 employers', 2 workers'), Glove Manufacture (1 employers', 1 workers'), Manufacture of Rubber Goods used in the Clothing Industry (1 employers', 1 workers'), Knit Goods and Hosiery Manufacture (2 employers', 2 workers'), Lace, Embroidery, and Ribbon, Elastic Fabric, and Trimmings Manufacture (2 employers', 2 workers'), Button Industry (2 employers', 2 workers'), Miscellaneous Clothing Accessories (1 employers', 1 workers'), Umbrella Manufacture (1 employers', 1 workers'), Trade in products named above (4 employers', 4 workers'), Artisans (3), Artists (1). The number of employers' representatives includes two representatives of business executives, one for industry and one for commerce."<sup>7</sup> In similar fashion, each of the other 21 category corporations included a president and from 15 to 68 members.

*The Functions of the Category Corporations* The functions of the category corporations were not very important at first. They were to furnish the government with information and advice on economic matters within their particular fields of interest, attempt through their conciliation boards to settle labor disputes which could not be disposed of by collective negotiations between employers' and employees' organizations, and help to prepare detailed plans for national economic self-sufficiency within their respective fields. During these early days, the category corporations operated more or less like the business pressure groups which exist in capitalistic countries. They would recommend the development of uniform market standards for particular commodities, additional aid for the export trade, the promotion of Italian dress fashions, the use of Italian-made motors in fishing vessels, the control of competitive imports, reduced transportation rates for individual commodities, marketing plans, and other similar plans.

Before long, however, the category corporations began to develop what became their most important function—that of drawing up groups of rules and regulations governing the economic conduct of their underlying firms and enterprises. In the short space of 3 or 4

<sup>7</sup> *Ibid.*, p. 112. Reprinted by permission of the President and Fellows of Harvard College.

years, these groups of rules and regulations came to cover such matters as the specification of fair and unfair competitive practices on the part of the individual firms, the control of prices, the prohibition of sales below "cost," production control, marketing control, limitations on the number of hours per week which productive facilities were allowed to operate in particular industries, and restrictions on the entry of new firms and the expansion of the productive facilities of old firms in individual lines of production. After being approved by higher authorities, these groups of rules and regulations drawn up by the category corporations were binding with the force of law on all the individual firms and enterprises under the supervision of the corporations. Thus, these groups of rules and regulations bore a strong family resemblance to the "codes of fair competition" which graced the American economic scene from 1933 to 1935 under the auspices of the National Industrial Recovery Act and the National Recovery Administration. Since the groups of rules and regulations were binding on the individual firms, and since they had to be approved by higher authorities, composed of leading Fascists, before becoming effective, it is clear that they constituted a vehicle by means of which the Fascist leaders and government could impose almost any kind or degree of control desired upon the productive activities of the individual firms and enterprises which were subsidiary to the category corporations. Actually, however, governmental control over productive activities was far from complete prior to the beginning of World War II.

*The National Council of Corporations* The 22 category corporations were at least nominally under the supervision of the National Council of Corporations which, after its reorganization in 1930, was intended to be the chief agency of economic coordination and control in the Fascist system—a kind of economic "general staff." Besides discussing all important matters of economic policy faced by the economy, it was to deal with problems such as "the organization of the syndical system, the national and regional coordination of employment, the adjustment of collective labor relations, and the formulation of rules for the coordination of the economic relations between the various branches of the nation's productive organism."<sup>8</sup> The groups of rules and regulations adopted by the

<sup>8</sup> *Ibid.*, p. 143. Reprinted by permission of the President and Fellows of Harvard College.

various category corporations were to be subject to its approval. In actual practice, the National Council of Corporations proved too large and unwieldy for the functions assigned to it, and its activities were limited to discussing and passing resolutions of a very general nature.

Most of the work of the National Council of Corporations was done by a smaller group known as the Central Corporate Committee, which was given the power to function in the place of the National Council in the intervals between its meetings. The Central Corporate Committee was composed of the Ministers of Corporations, Interior, Justice, Finance, National Education, Public Works, Communications, and Agriculture and Forests, the secretary general of the Fascist Party, other high Party officials and representatives of the Party in the category corporations, the presidents of the nine Fascist confederations (organizations of employers and of employees), the president of the National Institute of Cooperatives, high officials of the category corporations, and the secretary-general of the National Council of Corporations. The Central Corporate Committee actually approved the groups of rules and regulations adopted by the category corporations.

*The Ministry of Corporations.* At the head of the control organizations was the Ministry of Corporations, one of the departments of the Italian government.

The ministry is entrusted with such tasks as the approval of the by laws and the legal recognition of individual syndical associations [organizations of employers and of employees], the confirmation in office of all syndical officials, the supervision of the general activities and the financial administration of all syndical associations; the dismissal of syndical officials and the appointment of government commissioners for the reorganization of syndical associations, the determination of the amounts and the distribution of compulsory syndical dues, the drafting of labor and social security legislation, the registration of collective labor agreements and the arbitration of collective labor disputes, the planning and direction of the work of the individual corporations, the National Council of Corporations and the Central Corporate Committee, in each of which the Minister of Corporations is *ex officio* chairman, and the exertion of such persuasion and informal political pressure as may be necessary to insure collaboration of individual groups of workers or employers with the government. The ministry also supervises governmental unemployment exchanges, social insurance and social welfare organizations, and co-operative societies, collects and elaborates statistical information on questions of production and labor, edits several official periodical publications,

and carries out such activities of the former Ministry of National Economy as registration of patents and copyrights, inspection of factories, control of weights and measures, supervision of state and private insurance concerns, etc.<sup>9</sup>

It was in the Ministry of Corporations that some degree of economic planning was carried on by some method or other.

*The Estate of Industry and Trade in Germany* The National Socialists had been in power in Germany only about a year when their official organizations for controlling production were set up late in February, 1934. The control organizations in the field of industry and trade were placed under what was called the Estate of Industry and Trade. One of the top organizations in the Estate was the National Economic Chamber, which was composed of the seven National Groups into which the field of industry and trade was divided, the Provincial Economic Chambers, the local Chambers of Industry and Commerce, and the local Chambers of Handicrafts. The Minister of Economic Affairs appointed the director or leader of the National Economic Chamber and his deputies, and controlled the legal status of the Chamber. The leader of the Chamber was assisted by an advisory council composed of the leader of the Cooperative Council of Chambers of Industry and Commerce, the directors of the National Groups (and main groups in the field of industry and trade), directors of the Provincial Economic Chambers, four representatives of transportation, representatives of the Reich Food (Agricultural) Estate, representatives of the municipalities, and industrialists appointed by the Minister of Economic Affairs.<sup>10</sup> Alongside the National Economic Chamber was found the Cooperative Council (or Working Community) of Chambers of Industry and Commerce, which was made up of the local Chambers of Industry and Commerce which were scattered over the country.

*The Group Organizations* Under the auspices of the National Economic Chamber, the general field of German industry and trade was divided into a number of types of "group" organizations. In the first place, there were seven National Groups of industry and trade—namely, Industry, Trade, Banking, Insurance, Power, Tourist Industry, and Handicrafts. The National Group of Industry was further divided into seven Main Groups (1) Mining, Iron and

<sup>9</sup> *Ibid.*, p. 142. Reprinted by permission of the President and Fellows of Harvard College.

<sup>10</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 40.

Other Metal Ore Production, (2) Machine-Building, Technical, Optical, and Fine Mechanical Industries, (3) Iron, Plate, and Metal Wares, (4) Stone and Earth, Wood, Building, Glass, and Ceramics Industries, 5) Chemicals, Technical Oils and Fats, Paper and Paper-making, (6) Leather, Textiles, and Clothing, (7) Food-Products Industries. The other six National Groups were not divided into Main Groups, but all seven National Groups had other subsidiary organizations. The National Group of Handicrafts was divided into 50 National Guild Associations, while the other six National Groups were divided into some 46 Economic Groups, 328 Branch Groups, and 327 Sub-Branch Groups.<sup>11</sup>

By way of illustration, we may point out that, under the National Group of Industry, one Main Group was Mining, Iron and Other Metal Ore Production, under this Main Group, Economic Group A was Mining proper, and, under the Economic Group of Mining, there were Branch Groups, such as coal mining, lignite mining, iron-ore mining, and others. Under the National Group of Trade, Economic Group B consisted of Retail Trade, which in turn was divided into numerous Branch Groups, such as Tobacco Retailers, Shoe Retailers, Retailers of Musical Goods, Paper Retailers, and many others. Again, under the National Group of Banking, Economic Group E had to do with Credit Cooperatives, and was divided into Branch Groups of Agricultural Credit Cooperatives and Industrial Credit Cooperatives.<sup>12</sup>

*The Provincial Organizations.* Germany was, of course, divided into a number of geographical provinces. Each of the various Economic Groups, Branch Groups, and Sub-Branch Groups was allowed to organize itself into as many of these provinces as seemed desirable. In addition there were provincial guild organizations, which were under the National Guild Associations and the National Group of Handicrafts. All the provincially organized groups and provincial guild associations, together with the local Chambers of Industry and Commerce, were put together into Provincial Economic Chambers, of which there were 23 in all. The Provincial Economic Chambers were quite similar to the National Economic Chamber in organization. The leader of each Provincial Economic Chamber was ordinarily the Chairman of the local Chamber of

<sup>11</sup> F. L. Neumann, *Behemoth. The Structure and Practice of National Socialism*. New York: Oxford University Press, 1942, pp. 242-245.

<sup>12</sup> R. A. Brady, *The Spirit and Structure of German Fascism*, pp. 301, 302.

Industry and Commerce of the city in which the Provincial Economic Chamber was located

*The Local Organizations.* At the bottom of the heap, there were 100 local Chambers of Industry and Commerce, 70 Chambers of Handicrafts, and a number of Guilds and local organizations of the higher "groups." The German industrialists, business men, and handicraft producers belonged directly to the appropriate local organizations, and indirectly to the appropriate higher groups or handicraft organizations. Ordinary workers were not represented in any of these groups of industrialists and business men, but the employer groups in general were represented directly or indirectly in the Labor Front.

*The Organization of Transportation.* It was originally planned to bring all transportation agencies under the Estate of Industry and Trade, but eventually a separate organization, the Estate of Transportation, was set up for these agencies, presumably because some 80 per cent of the transportation enterprises were owned by governmental units, which made the problems of control somewhat different from those in the general field of industry and trade. The Estate of Transportation was divided into seven functional groups—sea-going shipping, inland shipping, motor transport, carrier services, rail vehicles, forwarding agencies, and auxiliary transport services. The Minister of Transport was the head of the Estate of Transportation, and he was advised and assisted by a National Transport Council composed of the leaders of the seven functional groups, representatives of the Reich Railway Office, Post Office, and Air Traffic, the General Inspector of Roads, and representatives of the Reich Food Estate, the Estate of Industry and Trade, the Chamber of Culture, the Labor Front, and the municipalities. As we have seen, the Estate of Transportation had representatives on the advisory council of the leader of the National Economic Chamber.

Such was the complexity of the original National Socialist organizations for the controlling of productive activities in the German economy. When it is remembered that all these organizations were superimposed upon the ordinary capitalistic organization of production in terms of single enterprises, partnerships, corporations, combinations, and cartels, we see why it was that the German capacity for organization excited the wonder, though not the admiration, of the rest of the world.

*The Functioning of the Control Organizations* Though we have examined the nature of the organizations originally set up by the National Socialists in the general field of production, we have not seen how these organizations operated prior to the period of active preparation for World War II On this subject there were significant differences of opinion among various outside interpreters of the National Socialist regime According to one school of thought, the entire set-up was under the domination and control of German industrialists and business men, with the government merely underwriting the ticket as prepared by private interests Other writers, after studying the same organizations and their functioning, reached the antithetical conclusion that German industrialists and business men not only did not dominate and control the entire economic situation but also were mere tools or pawns of the state

Still other writers, after studying the same organizations and their functioning, reached the perhaps more reasonable conclusion that a considerable amount of power and control was enjoyed by both business men and industrialists, on the one hand, and by the government on the other Sweezy said

The law does not give an exact definition of the functions of the individual organizations but transfers the functions and powers of the former business associations to the new units Any attempt to make clear cut divisions between the functions of these various formations would be attributing to them a definiteness which does not exist in the law The machinery that is thus set up to supervise industry and trade can be used to achieve almost any purpose so far as the formal provisions are concerned There are no longer any formal obstacles, in view of the leadership principle, to controlling the business man lock, stock, and barrel should the Minister of Economic Affairs see fit to do so By the same token there is nothing to prevent the business men from doing exactly as they please if they have any means for controlling the controllers The facts of the case probably represent a compromise between these two extremes<sup>18</sup>

A somewhat similar opinion is expressed by Reimann, who says

A superficial observer might easily claim that such a regime does not differ fundamentally from liberal capitalism, some governmental forms have changed perhaps, but the rôle and position of the capitalist or business man have remained what they were before Money still rules the world—democratic or fascist Such a conclusion would be just as false or incomplete as the opposite one, suggested in recent literature, that fascism is

<sup>18</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, pp. 41-43 Reprinted by permission of the President and Fellows of Harvard College

a new brand of feudalism in which the private capitalist has become merely the tool of the state—where absolute power has entirely taken the place of money power<sup>14</sup>

While power was nominally in the hands of governmental agencies and officials, business men used bribes, both direct and indirect, as the means of getting things done in Germany. Sometimes bribes were paid directly to Party men and sometimes indirectly through "legal advisers" or "contact men" who knew how to obtain concessions. As a matter of fact, the racket seemed to work both ways. Business men bribed and influenced Party officials and leaders, and the latter put the bite on business men. Business men, of course, did not always get exactly what they paid for, but it is well known that many Party officials achieved an amazing degree of economic success.

Laws and decrees are issued by the State according to immediate needs and emergencies. Officials, trained only to obey orders, have neither the desire, the equipment, nor the vision to modify rulings to suit individual situations. The state bureaucrats, therefore, apply these laws rigidly and mechanically without regard for the vital interests of essential parts of the national economy. Their only incentive to modify the letter of the law is in bribes from business men, who for their part use bribery as their only means of obtaining relief from a rigidity which they find crippling. So does corruption become a liberative force under fascism!<sup>15</sup>

At the absolute top, of course, the leaders of the Party and government were supreme, in the sense that no business men were big enough to prevail against Hitler and his immediate associates. This is not to say, however, that big business men had no influence with the National Socialist leaders.

Business men were unable to handle all their necessary dealings with the government in person, so they employed legal advisers or contact men.

Formerly the purchasing agent and the salesmanager were among the most important members of a business organization. Today the emphasis has shifted and a curious new business aide, a sort of combination "go between" and public-relations counsel is now all-important. His job—not the least interesting outgrowth of the Nazi economic system—is to maintain good personal relations with officials in the Economic Ministry.

<sup>14</sup> G. Reimann, *The Vampire Economy*. New York: The Vanguard Press, 1939, p. 28. Reprinted by permission of the publishers.

<sup>15</sup> *Ibid.*, p. 42. Reprinted by permission of the publishers.

where he is an almost daily caller, he studies all the new regulations and decrees, knows how to interpret them in relation to his particular firm, and is able to guess at what may be permitted or forbidden. In other words, it is his business to know how far one can go without being caught. He also develops special knowledge on how to camouflage private interests so that they appear to be "interests of the community" or of the state. He knows how urgent the demand of a State department or institution for a certain article may be and the effect of possible delays in delivery, and therefore, whether it will be possible to obtain a higher price or a bonus for speedy delivery. Such a contact man knows whether, when and how it is possible to obtain a special urgency certificate for a certain article and when to complain about the refusal of such a certificate. He also knows when to be satisfied with an ordinary certificate.<sup>10</sup>

The contact man knew which governmental officials were devoted Party men, and which were just ordinary army men, old fighters, or conservatives. A good contact man was indispensable even to a loyal Aryan firm.

With regard to the specific functioning of the individual organizations for the control of production, it may be said that actual policies and programs were formulated by the Minister of Economic Affairs and his advisers. The powers of the Minister of Economic Affairs extended through the leader of the National Economic Chamber down through all the functional and regional organizations. He had complete control over all nominations for office, deputy officers, council members, and the leaders of all the various groups. He removed officers at his discretion, made investigations, obtained reports, called meetings, and supervised the finances and conduct of all the control organizations. He had the power to determine whether cartel agreements or individual decisions were unfair, he could require outside firms to join a cartel if it seemed that market regulation by voluntary agreements were being defeated by too strong an emphasis of individual over collective interests, and could forbid the establishment of new enterprises and the expansion of existing establishments.

The programs and groups of regulations were enforced by means of the Cooperative Council of Chambers of Industry and Commerce and the local Chambers of Industry and Commerce. These policy-enforcing organizations had the task of keeping the individual

<sup>10</sup> *Ibid.*, pp. 44-45. Reprinted by permission of The Vanguard Press, New York.

enterprises and business men in line. The local Chambers of Industry and Commerce were set up as public corporations. They were legal representatives of the state and could levy taxes on their members. All the various Groups (National, Main, Economic, and Branch), the Provincial Economic Chambers, and the National Economic Chamber would examine and discuss programs and policies, take positions, form opinions, and give advice to the higher authorities. The various Groups and Chambers seemed to have no real power and authority. They were merely policy-debating and opinion-shaping organizations. The individual business men and industrialists wielded their influence, as previously suggested, primarily by "reaching" the high leaders and officials of party and government either before or after policies had been formed and controls had been set up.

*Later Additions to the Nazi Organizations for the Control of Production* As time went on, the power of the German government to control the productive activities of the economy was increased by the development of new organizations. The Second Four-Year Plan (largely for national economic self-sufficiency) was set in operation in 1937 with Goering and a small group of advisers at its head. Before long, there was quite a little overlapping and duplication between the activities of the leaders of the Second Four-Year Plan and those of the Ministry of Economic Affairs, and this led to a reorganization of the Ministry. In December, 1937, Goering announced the appointment of some 20 important executives and engineers as "leaders of defense industries" in aviation and it was disclosed that about the same thing had already been done for the munitions and shipbuilding industries. In 1938, special commissars or leaders were appointed for the construction, machine building, and automobile industries, and the same thing was done for the power industry in 1939. The functions of these leaders had to do with rationalization, extensions of capacity, and determination of priorities for these industries.

When World War II began in 1939, Hitler appointed a Council for National Defense, headed by the ever present Goering, with wide powers to control economic activities in the interests of the war effort. The Council carried on its work through regional defense commissars, provincial food and lumber bureaus, district economic offices, special commissioners to help out with the work of the Chambers of Commerce, and local food and economic offices. The

government decreed itself the power to conscript the productive facilities and raw materials of private enterprises and to require such enterprises to merge for purposes of pooling patents, erecting new plants, increasing exports, and increasing efficiency in general. Various associations of business men under the Estate of Industry and Trade and other Estates were required to exact contributions from their members to create funds with which to pay rent, interest, and depreciation charges of plants and factories which were compelled to close in the interests of the war effort.

The Council for National Defense was superseded early in 1940 by a new group, sometimes called the General Council for the War Economy, also headed by Goering. The new Council was given complete centralized control over all economic activities of the nation, including the affairs of private business, the war department, and the government. The Minister of Economic Affairs, who was formerly the head of all the organizations for the control of production, was definitely made subordinate to the new Council. Under Goering and the Council, the chief administrative agencies seemed to be the Four-Year Plan Office and the General Commissioner for Economics, who was the newly created chief over the Ministers of Economic Affairs, Labor, Finance, Food, and Forestry. The Four-Year Plan Office carried out its functions in part directly and in part through the agencies of the Ministry of Economic Affairs and general deputies for specific branches of industry and trade. Its functions had to do primarily with increasing the efficiency of particular industries and trades through measures of reorganization, standardization, and rationalization, though it seemed to share with the General Commissioner of Economics in the controlling of prices through the Price Commissioner, the Price-Forming Offices, and the Price-Supervising Offices.

The General Commissioner for Economics worked through the agencies of the Ministry of Economic Affairs and the other ministries under his general control. The agencies in question included Reich agencies for the rationing of raw materials and numerous distributing agencies for allocating raw materials to enterprises in specific branches of industry, leadership staffs for the economy in the various states or provinces, regional economic offices, and local economic offices, regional and local food offices for the rationing of food, and regional timber offices for the rationing of timber. Among these organizations, the regional economic offices apparently were of

considerable importance Subject to control from above, they could issue commands to the Provincial Economic Chambers, the local Chambers of Industry and Commerce, the Chambers of Handicrafts, the provincial "group" organizations, state mining agencies, offices for foreign trade, and currency offices They were expected "to secure production, to protect indispensable trades and handicrafts, to cooperate in safeguarding the supply of electric power, to execute measures concerning the consumption of coal, oil, rubber, textile materials, and soap, and to organize the collection of used materials"<sup>17</sup>

Since these new and strong control agencies were set up without disbanding those which had previously existed, it is easy to conclude that the position of the German business man or industrialist in the war economy was a rather complicated one In this section of our study, we have been dealing for the most part with organizations for the control of production, but we should not make the mistake of assuming that the German business man was responsible only to such organizations Actually he was responsible to or was influenced by a great and bewildering variety of governmental and government-sponsored organizations in other phases of economic activity, as we shall see in later chapters

*Advantages of Fascist Controls over Production* From the point of view of attaining efficiency in production, there are some things to be said for the types of controls over production used in Italy and Germany In the first place, they gave the government the necessary power to direct production and to attain its desired objectives without taking the customary capitalistic incentives away from industrialists and business men That is, private individuals continued to own and operate the industries and businesses of the countries and to be motivated by considerations of profit and loss This situation may readily be better, from the point of view of efficiency, than the one in which the governments own and operate the industries and businesses, and business men are reduced to the status of governmental employees on a salary, while governmental control over production may be as complete in the one case as in the other

The industrialists and business men of Germany and Italy, or at least the larger enterprises and combinations of enterprises, seemed

<sup>17</sup> F. L. Neumann, *Behemoth: The Structure and Practice of National Socialism*, p. 249

to fare rather well under fascism. The fascist objectives of conquest, glory, and stabilization of the regime appeared to be quite consistent with the desires of big business for full and profitable utilization of productive facilities. There was a strong, government-sponsored concentration movement in industry and business in each country, thousands of small industrialists and business men were eliminated, and many new combinations and cartels were formed. Large firms and combinations were assigned the responsibility for founding and operating new firms and industries made necessary by the self-sufficiency programs. The payment of dividends by corporations was strictly limited, but this affected only the distribution of profits and did not set any limit on corporate profits as such. Even under strict price control, the enterprises with the greatest efficiency and lowest costs could still make plenty of money, though how much of their profits they retained after paying taxes was another matter. Finally, the fascist policies with respect to labor were always quite favorable for the employers.

The results, in terms of profits, may be seen in the German situation. Statistics for the largest 46 per cent of German corporations, which owned roughly 92 per cent of total corporate capital, showed that the average profit ratio (net earnings as a percentage of net worth) increased from -10.59 per cent in 1931 and -3.65 per cent in 1932 to 4.22 per cent in 1935, 5.30 per cent in 1936, 6.16 per cent in 1937, and 5.66 per cent in 1938.<sup>18</sup> That production did not become less profitable for large German businesses after the beginning of World War II is suggested by the report that, by the middle of 1942, 833 large corporations had increased their capital from 4.9 to 7.8 billion marks by means of the reinvestment of profits.<sup>19</sup> Such statistics, of course, did not tell us what had happened to the smaller corporations which made up 54 per cent of the total number but owned only 8 per cent of total corporate capital, nor did they disclose the fate of unincorporated German business men.

The concentration and combination movement was another factor with implications for the efficiency of production in the fascist countries. In Italy the government sponsored numerous cartels or combinations in important industries, including the ship-building, iron and steel, chemicals, rayon, railway equipment, cement, and electric bulb industries, and permitted the formation

<sup>18</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 73.

<sup>19</sup> *In Fact*, January 25, 1943, p. 3.

of numerous agreements among the firms in individual industries for purposes of price fixing, market sharing, and production control. The government also facilitated many business mergers, through tax concessions and otherwise. In the ten years before 1927, there had been only 160 business mergers in Italy. From the middle of 1927 to the middle of 1929, there were 221 mergers involving a total capital of 10 billion lire and resulting in the elimination of 878 firms. From 1930 to 1932, there were 244 additional mergers involving 13 billion lire and 364 firms. By 1935, one-fourth of the total number of Italian corporations controlled 95 per cent of all corporate capital, and 118 firms (amounting to one-half of one per cent of the total number) controlled 48 per cent of total corporate capital.<sup>20</sup> Monopolies and quasi-monopolies became relatively common.

In Germany, the total number of corporations was 5518 in 1938. It had been 11,690 in 1928. Over the same period, the corporations with a capital of 5 million marks or over declined in number only from 750 to 616. These giant corporations, which had controlled about 56 per cent of the total capital of all corporations in 1928, controlled 77 per cent in 1938, although they were only 11 per cent of the total number of corporations at that time. From 1938 to 1939, the total number of corporations declined further from 5518 to 5353, but their total capital increased from 17.75 to 20.34 billion marks.<sup>21</sup>

In addition to the large number of mergers, there was a considerable development of cartels in Germany under National Socialism. In 1933, the powers of the cartel court were transferred to the Minister of Economic Affairs, who could decide whether cartel arrangements and individual decisions were unfair. Again, the Minister was given the power to make outside firms join cartels, and he could prohibit the establishment of new firms and the expansion of existing firms. These powers were used on numerous occasions. The Minister could compel or prevent changes in cartel agreements, restrict the use of existing productive facilities, and establish the rights and duties of cartel members. Since many of these restrictions were capable of operating to the benefit of members of cartels, the attractiveness of the cartel form was increased.

<sup>20</sup> C. T. Schmidt, *The Corporate State in Action*. New York: Oxford University Press, 1939, pp. 121-122.

<sup>21</sup> *Foreign Commerce Weekly*, January 4, 1941, pp. 13-14.

and the number of cartels increased from 2000 in 1925 to 2200 in 1935 and 2500 in 1936.<sup>22</sup> Many additional cartels were formed in later years.

Besides those who were absorbed by larger firms, thousands of small industrialists and business men were forced out of business because they could not continue operating under the officially set prices for their products, because they could not obtain funds for modernizing their plants, because they could not secure stocks of raw materials or finished products from the rationing or distributing boards, or because their workers were shifted bodily to other plants in the same industry or in other industries. The elimination of weak and inefficient producers in various fields, or their absorption by larger and more efficient concerns, may have contributed something to the overall efficiency of production in the fascist countries. Moreover, the efficiency of governmental control was probably increased, since the government could deal more effectively with a few large firms than with many small ones in a given industry.

Besides the factors which have been mentioned, the fascist economies like other completely controlled systems, could go far toward the elimination of the so-called competitive wastes in production. Through the combination movement and otherwise they could cut down the duplication of productive facilities and idle productive capacity. They could reduce the undue proliferation of styles, shapes, sizes, and varieties of goods and concentrate on a smaller number of standardized varieties. They could limit the amount of time, effort, and money devoted to advertising and selling activities, and they could discourage the tendency to waste which is often present in the competitive exploitation of natural resources. Finally, they could keep their productive systems operating at high and relatively stable levels and avoid the depressions which are likely to occur at times in uncontrolled economies.

*Disadvantages of Fascist Controls over Production.* On the other hand, there were a number of factors in the fascist systems for controlling production which were less favorable from the point of view of efficiency. One, of course, was the overwhelming complexity of the controls and control organizations. Foreigners in Germany before the war were amazed to discover, for example, that the government found it necessary to regulate such a simple profession as chimney sweeping by means of 24 pages of orders printed in fine

<sup>22</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 94.

type.<sup>23</sup> They could scarcely believe that in modern Germany the house-wrecking business found "its place in the Nazi organization and regulation of the national economy under this title 'Special Sub-Group-for-Businesses-Engaged-in-Wrecking-and-Tearing-Down of the Special-Group-for-Businesses-Engaged-in-Dealing-in Old-and-Waste-Materials in the Group-for-Businesses-Engaged-in-the-Whole-sale-Import-and-Export-Trade'"<sup>24</sup> And their feeling amounted almost to consternation when they read a report in the newspaper concerning a meeting of representatives of the "Special-Sub-Group for - Businesses - Engaged-in-Producing-and-Dealing-in - Technical-Chemicals-and-Technical-Raw-Materials" with representatives of the "Special-Sub-Group-for - Businesses-Engaged-in-Producing-and-Dealing-in-Vegetable-Drugs" of the "Special-Group-for-Businesses-Engaged-in-Producing-and-Dealing-in-Technical-Oils-and-Fat-Drugs-and-Rubber" of the "Group-for-Businesses-Engaged-in-the-Whole-sale-Import-and-Export-Trade"<sup>25</sup>

Not infrequently the complexity of the National Socialist control organizations must have been greatly confusing to the German business men themselves. But, it has been said, "There is only one formula the nazis seem to know for dealing with this confusion whenever the situation threatens to get completely out of hand, they set up a new office to coordinate and rationalize the ones already in existence. In time, even the coordinators and rationalizers become so numerous and so confusing—and confused—that coordinators of the coordinators have to be appointed to rationalize the rationalizers."<sup>26</sup> As someone said, after a leading Nazi official was reported to have lost his mind "It was not surprising that a man in a position of responsibility in the nazi economic and financial system should go mad—the surprising thing about it was that anyone should have noticed that he was mad."<sup>27</sup>

Amid such a welter of control agencies, and especially when, as sometimes happened, the power to control a particular phase of economic life (for example, prices) was divided among four or five different agencies of the government, business men in the fascist countries had difficulty in deciding just who their bosses were or

<sup>23</sup> W R Deuel, *People Under Hitler* New York Harcourt, Brace and Company, Inc, 1942, p 339

<sup>24</sup> *Ibid*, p 339 Reprinted by permission of the publishers

<sup>25</sup> *Ibid*, pp 339-340 Reprinted by permission of the publishers

<sup>26</sup> *Ibid*, pp 337-338 Reprinted by permission of the publishers

<sup>27</sup> *Ibid*, pp 336 Reprinted by permission of the publishers

where they should look for guidance or orders. Delays in getting decisions, or in securing permits to do this or that, were troublesome in the extreme. Business men and industrialists were given fat sheaves of regulations to comply with and the ordinary individual would find it impossible even to understand all the regulations, let alone to comply with them, and this was especially true when various regulations conflicted with each other.

The government also furnished business men and industrialists with an almost endless succession of forms, reports, and questionnaires, all to be filled out post haste and usually in quintuplicate or septuplicate. The amount of "paper work" which resulted was practically beyond description. In short, the fascist policy seemed to be to tie the business man hand and foot and then tell him to go ahead, operate his business, and make profits. The result would be either that the business man would become hopelessly enmeshed in regulations and red tape so that he could not operate his business efficiently or else that corruption, evasion of regulations, black marketing, and bribery of government officials would flourish so that businesses might continue to operate. In either case, the results desired by the fascist leaders would not be completely obtained.

*Italian Industrial Production.* Turning now to industrial production, in Table 5 we present statistics on the output of a few important industrial commodities in Italy after the advent of fascism.

TABLE 5  
PRODUCTION OF IMPORTANT INDUSTRIAL COMMODITIES  
IN ITALY IN SELECTED YEARS

Item	Unit	1922 Output	1927 Output	1932 Output	1937 Output	1940 Output
Iron and steel	Thousand tons	1,046 0	1,721 8	1,497 1	2,086 9	2,500 0
Perphosphates	Thousand tons	947 6	1,371 5	661 6	1,333 2	
Sulphuric acid	Thousand tons	485 4	820 0	562 0	1,642 1	
Electric power	Billion kilowatt-hours			8 4	10 3	14 4
Raw silk	Thousand kilograms					17 1
Rayon	Thousand kilograms	3,989 8	5,009 8	3,927 0	2,861 0	
Cotton yarn	Thousand tons	2,593	24,406	34,038	124,388	
Cotton cloth	Thousand tons	154 3		169 1	170 4 <sup>a</sup>	
		100 9	116 0	73 2	79 6 <sup>a</sup>	

SOURCES: W G Welk, *Fascist Economic Policy*, pp 198-200, *The Economist* (London), May 17, 1941, p 657.

<sup>a</sup> 1936 output

Most of these statistics show the effect of the boom period from 1922 to 1927, the great depression that followed, and the recovery of the 1930's Since productive activities in Italy came under complete governmental control only in the last few years of the Fascist regime, we should not expect the statistics to indicate anything very significant concerning the effects of the Fascist control organizations on industrial production With the beginning of the war, Italy went under an almost complete statistical blackout, and only occasional figures for production leaked out

*German Industrial Production* Under the influence of recovery from the great depression and the armaments and self-sufficiency programs, industrial production in Germany increased by leaps and bounds in the first several years under National Socialism The index numbers of industrial production presented in Table 6 show that industrial production in 1938 was more than double that of the depression year of 1932 However, they also indicate that the production of capital goods in 1938 was about three times as great as in 1932, while the production of consumers' goods was less than 50 per cent greater in 1938 than in 1932 Since these index numbers use 1928 as the base year, it is also obvious that, while the production of capital goods in 1938 was about 36 per cent greater than in 1928, the production of consumers' goods was only about 8 per cent greater However, even these figures should not be used with too great enthusiasm One estimate of German national income claims that per capita income, as deflated for changes in the value of money, increased only 23 per cent from 1932 to 1938 and only 18

TABLE 6

INDEX NUMBERS OF INDUSTRIAL PRODUCTION, CAPITAL  
GOODS PRODUCTION, AND CONSUMERS' GOODS PRODUCTION IN  
GERMANY, 1932-38

Year	Index of Industrial Production (1928 = 100)	Index of Capital Goods Production (1928 = 100)	Index of Consumers' Goods Production (1928 = 100)
1932	58 7	45 7	78 1
1933	65 5	53 7	82 9
1934	83 3	77 2	87 6
1935	95 8	99 4	91 0
1936	106 7	112 9	97 5
1937	116 7	126 0	102 8
1938	124 7	135 9	107 8
1939 (May)	130 1	148 9	116 1

SOURCE Institut für Konjunkturforschung, *Statistik des In- und Ausland*

per cent from 1929 to 1938 Moreover, most of the increase in the national income went into the armaments program and it is estimated that, if we eliminate the goods produced for the armaments program, per capita income, including both civilian consumption and ordinary civilian investment, increased only about 8 per cent from the depths of the depression<sup>28</sup>

*Fascist Industrial Production in Wartime.* In the period of World War II Italian industry had all it could do to hang on and keep running It was seriously handicapped by the loss of foreign markets and sources of supplies and materials and became more and more dependent upon whatever the German economy could spare Germany was apparently somewhat better prepared than Italy at the beginning of the war, and of course her successes in the early years of the war provided her with considerable additional amounts of materials, supplies, equipment, and machinery However, as the war wore on, and especially as allied air attacks on Germany became increasingly severe and widespread, German industry also had grave difficulty in maintaining production

In both economies, of course, productive activity was concentrated increasingly in war industries and governmental controls over production became more and more direct, specific, and severe Industries producing consumers' goods were permitted to run only a few hours per week or were even closed down altogether at times Scarce materials were severely rationed among industries and firms, with large proportions being reserved for use in war production Thus, firms producing consumers' goods, even though they had permission to operate, were sometimes unable to do so because they lacked necessary materials Firms were required to report their stocks of scarce materials, the consumption of these stocks, and their prospective needs for later periods Intensive drives were carried on to collect and reuse scrap and waste materials Industries producing consumers' goods were required to limit themselves to the production of one or two standard types of goods and were made to use considerable amounts of ersatz or substitute materials in their production Finally, manufacturers were often required to report their stocks of finished products and reserve considerable portions for governmental use

Heavy penalties were provided for violations of these various controls Individuals could be sentenced to death for withholding large

<sup>28</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, pp. 204-205

amounts of goods from normal consumption or for the destruction of raw materials, agricultural products, or industrial commodities. Fines and imprisonment were provided for small-scale hoarding, the failure to deliver requisitioned goods, false bookkeeping entries to avoid compulsory pooling or requisitioning, the use of goods for other than allotted purposes, dealing in violation of rationing regulations, obtaining rationed goods in excess of allotted quantities, and offering goods for sale at higher than official prices.<sup>20</sup> In spite of all controls and penalties, however, industrial production in the fascist countries eventually proved entirely inadequate for the attainment of the objectives which had been set up by the fascist leaders.

#### QUESTIONS

- 1 How is production controlled in the nationalized industries in Britain under partial socialism? Explain
- 2 What are the bases for the hopes of the Labor Government that a high degree of efficiency will be attained in the nationalized industries in Britain?
- 3 "Governmental control over private industries and businesses is very complete and severe in Britain under partial socialism." Show whether you agree
- 4 Comment on the results obtained in the field of industrial production in Britain under partial socialism
- 5 Explain the nature of the "category corporations" in Italy under fascism
- 6 How were the category corporations used as instruments of governmental control over production? Explain
- 7 Explain the relationships which existed between the various organizations which operated under the auspices of the Estate of Industry and Trade in Germany under fascism
- 8 Distinguish between National Groups, Main Groups, Economic Groups, and Branch Groups in the fascist organization for controlling production in Germany
- 9 "The most striking feature of the fascist organization for controlling production in Germany was its extreme complexity." Explain
- 10 "The control of production under fascism in Germany was really divided between business men and the government." Do you agree? Explain
- 11 "With the beginning of World War II, the power of the German government to control the productive activities of the economy was increased through the development of new organizations." Explain
- 12 "From the point of view of attaining efficiency in production, there

<sup>20</sup> *Foreign Commerce Weekly*, September 13, 1941, p. 34.

- were some things to be said for the types of controls over production used in Italy and Germany under fascism?" Show whether you agree.
- 13 "There was a strong concentration and combination movement in industry in both Italy and Germany under fascism." Explain and illustrate.
- 14 "Controlled economies of the fascist type can go far toward eliminating the competitive wastes in production which often exist in capitalistic systems." Explain.
- 15 What were the disadvantages of the kinds of controls over production that were used in Italy and Germany under fascism? Explain.
- 16 "In the period of World War II, governmental controls over production in Italy and Germany became more direct and more specific than formerly." Explain.
- 17 "The incentives in a fascist system of controlled production may be superior to those in a socialist system." Do you agree? Explain.
- 18 "In both Italy and Germany under fascism, governmental control over productive activities was achieved by superimposing control agencies upon what was basically a capitalistic organization of production." Explain and illustrate.

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## CHAPTER 9

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### **A G R I C U L T U R E**

#### *Agriculture under Capitalism*

IN theory, agriculture is to be organized and operated very much like any other industry in a capitalistic economic system. Individuals are free to become farmers, to put into agricultural production as large quantities of the productive factors as they can obtain, to produce any crops they like in any quantities that seem desirable, to organize their businesses as single enterprises, partnerships, corporations, or cooperative enterprises, and to operate their businesses in pursuit of private profits. In practice, in the United States, corporations are comparatively rare in agricultural production. The firms or enterprises in agriculture are more numerous and smaller than those in manufacturing and other industries. Large-scale farming is practiced, of course, but the large-scale farm is much smaller than the large-scale firm in other industries. Conditions are more nearly competitive in agriculture than in most other lines of production and the individual farmer is quite powerless to affect the prices which he receives for his products or the prices which he must pay for productive factors or for finished manufactured goods. In the absence of monopolistic tendencies, the farmer is unable to pursue profits by restricting rather than expanding output or by maintaining rigid prices through periods of good and bad business. Since the farmer owns a considerable part of the productive agents which he employs and since he has rather important fixed costs in the form of interest and taxes, he is likely to continue to operate at or near full capacity even when market conditions are unfavorable, in order to obtain some return from the productive agents which he owns.

*The Agricultural Problem in the United States*. With conditions differing considerably as between agricultural production and most other fields of production, it is a rare capitalistic economy which has

not had an "agricultural problem" in recent years. The United States has been no exception to the rule in this respect. Agricultural production in the United States increased rapidly during and after World War I under the influence of a tremendous domestic and foreign demand for farm products, the mechanization of agriculture, improved methods of cultivation, the bringing of much new land under cultivation, specialization in the raising of money crops for the market, and the reduced need for land to raise feed crops for farm animals. Exports of agricultural products increased sharply and the gross farm income of the country more than doubled from 1914 to 1919. In 1918, the prices received by farmers stood at 202 (with 1909-14 as the base) while the prices paid by farmers were only up to 176. In 1919, these two index numbers were 213 and 202 respectively.<sup>1</sup> Therefore, the farm income of this country increased both absolutely and in relative purchasing power during the war and early postwar years.

After World War I was over, agricultural production improved in the former belligerent countries of Europe, and some of them attempted to increase agricultural production far beyond the prewar levels. American farmers also faced increased competition from other agricultural areas in the markets of the world. Our high tariff policy after the war hindered our farmers in their efforts to retain export markets, and the eventual and inevitable curtailment of the large loans which Americans had been making to other countries had a similar effect. Changes in the American diet and the adoption of prohibition are supposed to have had a depressing effect on the domestic market for some farm products. However, in the face of unfavorable conditions of demand, American farm acreage and production were very well maintained both in the 1920's and during the years of depression after 1929.

As a result, the American farmers were greatly distressed by the "scissors problem," or the great and growing disparity between the prices which farmers received for their products and the prices which they had to pay for the products of other industries. In the "prosperous" days of 1929, prices received by farmers stood at 146, while those paid by farmers were at 153 (on the basis of 1909-14 prices as 100). In 1931, prices received by farmers were at 87, while those paid by farmers were at 124, and in 1932 the two index num-

<sup>1</sup> *Statistical Abstract of the United States, 1935*, pp. 680-681.

bers were 65 and 107, respectively.<sup>2</sup> Although the farm problem was really a group of closely related problems, which included soil erosion, dust and flood control, the migration of farm workers, farm debts, farm credit, tax delinquency, share-cropping, farm tenancy, and many other matters, the main farm problem had to do with agricultural prices and income.

*Solving the Agricultural Problem Under American Capitalism*

Occasional attempts to deal with the American agricultural problem were made during the 1920's, and in the great depression after 1929 the farm situation became so serious that drastic governmental action seemed to be required. However, the federal government of the United States, as the government of a capitalistic system, was greatly handicapped in dealing with the farm problem. It could not take over and operate American agriculture, it could not compel American farmers to band together into large-scale cooperative farm enterprises, and it could not directly withdraw large quantities of land and other productive instruments from agriculture or lift large numbers of farmers bodily from agriculture and transplant them in industry. While the program of the Roosevelt Administration for dealing with the agricultural problem embodied quite a number of phases, the principal part involved the payment of cash benefits to farmers to get them to operate their productive facilities at a rate well below normal capacity. The purpose of the program was obviously to get the farmers better prices and a greater total income for their restricted outputs in addition to the benefit payments which they received.

While the exact results of the operation of the Agricultural Adjustment Act of 1933 and Agricultural Adjustment Administration have never been determined, the Act was under heavy criticism during its short life. It was found unconstitutional by the Supreme Court in January, 1936. The Agricultural Adjustment Administration continued to exist and, in February, 1936, a previously existing Soil Conservation Act was amended and enlarged for the purpose of permitting a continuation of the crop-control program by connecting it with an attempt to deal with problems of soil erosion. A new Farm Act was passed in 1938 that provided for the continued operation of the Soil Conservation Act, and its payments to farmers, in normal times. In years of overproduction, however, more stringent methods of control, involving acreage allotments, marketing quotas,

<sup>2</sup> *Ibid*.

discriminatory commodity loans, and other devices, go into effect for the purpose of controlling production and maintaining prices

Except to the extent that the government has been buying up and withdrawing from use some millions of acres of low-grade farm land, it must be said that the government's program has not been successful in providing a long-run solution of the American agricultural problem. In other words, it has succeeded only in decreasing output by lowering the rate of operation of existing farm productive facilities, and has not resulted in the withdrawal of large quantities of productive facilities and farmers from agriculture. During World War II, the foreign and domestic demand for American farm products increased sharply once more and the farmers enjoyed great prosperity. In spite of expanding production, the prices of farm products rose both absolutely and relatively to the prices of other goods, and farm income rose to new all-time record levels.

The wartime problem in agriculture was to secure enough farm products rather than to restrain production and prevent surpluses, so that various controls provided by the Act of 1938 could be largely relaxed. However, payments to farmers under the Soil Conservation and Domestic Allotment Act of 1936 went forward as usual during the war period. In addition, it was thought necessary to take certain steps to stimulate agricultural production. The most important of these was a series of acts which placed price floors under agricultural products and promised a continuance of parity price guarantees into the postwar period. The agricultural situation in the United States remained favorable in the first three years after the war, but it is still possible that the agricultural problem will spring up again in all its former glory later on. As we shall see, the governments of the controlled economies are able to use somewhat more effective, though harsher, methods than those employed by the government of a capitalistic economy in dealing with problems of agricultural maladjustment.

### *Agriculture in Soviet Russia*

*Agriculture under Socialism and Communism* Comparatively little is said in the prospectus of modern socialism as an ideal theoretical system concerning the organization and operation of agriculture. We noted in Chapter 7 that a modern socialistic system might not be in any great hurry to socialize agricultural production,

and that it might permit all or a large part of agricultural production to be operated by cooperative enterprises or even by private individuals for a long time. We have also referred to some of the devices which a socialistic economy could use for controlling such private or cooperative production and bringing it into adjustment with the general economic plans for the whole economy. Since they anticipate no very serious agricultural problems in the system which they advocate, modern socialists have little to offer in the way of detailed suggestions for handling agricultural problems under socialism. For concrete details as to the organization, operation, and problems of agriculture in a socialistic economy, we must refer to the experience of Soviet Russia. It is also true that very little of a specific character has been said or written on the subject of the operation of agriculture under a system of modern communism.

*Early Conditions in Russian Agriculture.* Russia at the time of the revolution was predominantly an agricultural economy, but her peasant system of agriculture was most unproductive and inefficient. There had been as high as 35 bad crop years in 50, and there were only three good harvests in the first 10 years of Soviet rule. The individual peasant's land area was small and tending to become smaller. Moreover, each peasant had several small strips of land to cultivate and the strips were often located miles apart. There was little incentive to improve the land because of periodic redistribution of the peasant holdings. A third of the peasants had no iron plough and a fourth of them had no horse or ox. Little manure was used and almost no artificial fertilizer. There was virtually no rotation of crops and almost no weeding or cultivation. Grains were still reaped with the hand sickle and threshed with the flail. The peasants had little direct connection with the revolution and all it meant to most of them was a vague notion that they would get more land. The only people in agriculture who were sufficiently intelligent and well trained to serve as the basis for making a system of socialized agriculture operate successfully were out of sympathy with the new regime.

On the basis of these conditions, the Soviet regime faced a most difficult problem in converting Russian farms into efficient large-scale units capable of furnishing large surpluses of food for the growing urban and industrial population and large quantities of raw materials for industry. During the early years of War Communism, the system of "food collections" under which the govern-

ment seized most of what the peasants produced caused a great decline in agricultural production. The land under cultivation declined from 91 to 54 million hectares, the grain crop fell from 65 to 27 million tons, and the yield per hectare slumped from 7.08 centners to 4.80.<sup>8</sup> There was some revival of Russian agriculture under the New Economic Policy (1921-27). However, there were severe restrictions on the right of peasants to sell their produce on the open market, on the size of peasant land holdings, and on their right to rent land or hire help, and the government required large compulsory deliveries of farm produce at low prices. Since the prices that they could get for their goods were low and the prices that they had to pay for manufactured goods were high, the Russian farmers, like those of other countries, suffered from the well-known "scissors problem." The farmers would not furnish large quantities of food and materials for the urban and industrial population so long as manufactured goods were scarce and high priced, and Russian industries, faced with a shortage of food and materials, could turn out only a relatively few, high-cost goods for the farmers.

*The Collectivization of Russian Agriculture.* In spite of the unfavorable conditions existing at the time, the First Five-Year Plan (1928-32) counted upon the rapid development of agricultural production. On the other hand, it was intended to go slowly in the matter of socializing agriculture, and the plan called for at least 75 per cent of the marketable farm produce to come from the privately owned sector of agriculture even at the end of the five-year period. However, agricultural conditions remained most unfavorable. The total amount of land under cultivation and the size of leading food and industrial or technical crops remained below the 1913 level. Little if any progress was made in livestock raising, and there was no grain for export in 1928. The harvest in 1929 was poor but the government nevertheless undertook to seize 13.9 million tons of grain. Peasant resistance was strong. Crops were left to rot in the fields or were burned or hidden from the collectors after the harvest. As a result, the leaders decided to bring agriculture under collectivization much more rapidly than had been originally planned.

In 1930, some 25,000 Communists were sent out into the country with absolute powers to bring about collectivization. There followed

<sup>8</sup> N. de Basily, *Russia under Soviet Rule*. London: George Allen and Unwin, Ltd., 1928, p. 255. One hectare = 2.47 acres, and one centner = 220.46 pounds.

what is usually called the liquidation of the "kulaks," or well-to-do farmers. Most descriptions of this process are harrowing, to say the least.<sup>4</sup> Thousands of resisting peasants were shot, and millions of others (some say four or five millions)<sup>5</sup> were evicted from their homes and lands. Their possessions were seized, even their warm clothing was taken away, and they were loaded into unheated cattle cars for transportation to Siberia or some other remote region where they died like flies from cold, hunger, and exhausting labor. Sometimes only the men were taken away, and the women and children were left at home to starve. Nor was the liquidation limited to the really prosperous peasants. Where no kulaks actually existed, some were invented, and anyone a little better off than his neighbors was likely to suffer the sad fate of becoming a kulak in the eyes of the Communists. This meant, in effect, that hard work and initiative were penalized wherever found, the incentives of the remaining peasants were destroyed, and exactly those peasants were eliminated whose skill, knowledge, and industry might have led to the development and improvement of Russian agriculture.

The remaining peasants were driven into collective or cooperative farms and were supposed to pool their productive instruments and livestock. But they regarded this pooling as expropriation and many peasants killed their livestock and ate it or sold it and hid the money. Since they were required to deliver their surplus agricultural products to the government, the newly created collective farmers decided to raise just enough produce for themselves. But the government took its compulsory deliveries anyhow and the peasants were left to starve on the remainder of the crops. Some estimates have it that from 5 to 10 million persons perished from starvation during the famine conditions of 1931 and 1932.<sup>6</sup> Later on in the chapter, we shall see in greater detail just what happened to agricultural production and livestock on hand during the operation of the First Five-Year Plan. Just at present we are more interested in the collectivization process itself.

In 1928, state farms had used 1.7 million hectares, or 1.5 per cent of the total cultivated area, and collective farms had used 2.6 million hectares, or 2.2 per cent of the total. Individual peasants still culti-

<sup>4</sup> See, for example, T. Utley, *The Dream We Lost*, pp. 50-55, and A. Yugow, *Russia's Economic Front for War and Peace* (New York: Harper and Brothers, 1942), p. 45.

<sup>5</sup> M. T. Florinsky, *Toward an Understanding of the U.S.S.R.*, p. 197.

<sup>6</sup> F. Utley, *The Dream We Lost*, p. 55.

vated 108.7 million hectares, or 96.3 per cent of the total.<sup>7</sup> By the end of 1931, 60 per cent of the peasant farms had been collectivized, and about 78 per cent of the cultivated area was collectivized by the end of the five-year period.<sup>8</sup> Just before World War II began, there were something over a million individual farmers, but they cultivated only about 900,000 hectares, or 0.6 per cent of the total cultivated area. The state farms (*sovkhosy*) operated on 12.4 million hectares, or 9.1 per cent of the total cultivated area, and the collective farms (*kolkhozy*) had 117.2 million hectares, or 85.6 per cent of the total.<sup>9</sup> The rest of the land was cultivated by individual collective farmers as their personal homesteads, and by workers and employees in other industries.

*The State Farms.* In examining the present organization of Soviet agriculture, we turn first to the state farms. As of January 1, 1947, there were 4234 of these farms.<sup>10</sup> How much of their formerly cultivated area has been actually returned to cultivation since the war is not known but, on the basis of their old total cultivated area, their average size would be around 2929 hectares, or 7235 acres. Most of the state farms are highly specialized agricultural units. For example, there were in 1938 some 471 grain farms, 407 fruit and grape farms, 755 cattle farms, 650 pig farms, 200 sheep farms, 119 horse farms, 180 sugar beet farms, 95 poultry farms, 100 farms growing special crops (tea, tobacco, rubber plants), and 836 suburban truck farms and miscellaneous farms.<sup>11</sup> The state farms raising particular products are gathered together under trusts which are very similar to those in industry, and the trusts are in turn responsible to the Ministry of State Farms.

The internal organization of the state farms is comparatively simple. All the land, buildings, machinery, and productive equipment in general is owned by the government (or by the people as a whole through the government), and the farms are managed by government-appointed directors. The employees of the state farms are simply wage-workers, who have no more direct interest in the enterprises than the ordinary industrial workers have in their factories and have no claim on the products of the state farms. The

<sup>7</sup> *Russian Economic Notes*, Number 21, pp. 15.

<sup>8</sup> B. Brusilov, *Economic Planning in Soviet Russia*, p. 156; M. T. Florinsky, *Toward an Understanding of the USSR*, pp. 159-160.

<sup>9</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 327.

<sup>10</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 54.

<sup>11</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 334.

workers and their families have the use of various common facilities, such as living quarters, dining rooms, day nurseries, kindergartens, and various other educational and recreational facilities, and they may own small numbers of domestic animals, but no draft animals. The workers are quite well treated apparently in the matter of wages. In 1937, when the average wage in industry was 2772 rubles per year, a skilled worker on a state farm was getting from 4000 to 5000 rubles annually.<sup>12</sup> An attempt is made to pay the workers on a piecework basis, and each state farm has a "director's fund," similar to those in industry, into which portions of planned and unplanned profits are paid for use in connection with various local benefits and improvements. The full-time workers on the state farms number a little less than two millions.

The early state farms were made from old landed estates, formerly uncultivated areas, and reclaimed land, and did not result from the combining of collective farms or the holdings of individual peasants. Later some state farms were made out of land, formerly cultivated by individuals, which had not yet been assigned to collective farms. The state farms were intended to increase agricultural production by enlarging the land area under cultivation, by utilizing modern efficient methods, and by serving as experimental stations and modern agricultural centers to give an example to the other agricultural enterprises of the country. As originally set up, the state farms were extremely large. In 1930, the state grain farms averaged 116,000 hectares or about 286,500 acres.<sup>13</sup> Not only did the individual farms embrace hundreds of thousands of acres, but they operated "with huge fleets of combines, batteries of searchlights for night work, radios sending orders to the harvesters encamped for weeks in the distant fields, air planes bringing their medicines, magazines, and entertainers."<sup>14</sup>

The Soviet leaders invested large sums in the state farms and they became mechanized to a much greater extent than the collective farms. On the state farms, 94.5 per cent of the plowing, 95 per cent of the hauling, and 80 per cent of the other work was done by machinery even before World War II.<sup>15</sup> They received the best

<sup>12</sup> A. Yugow, *Russia's Economic Front for War and Peace*, New York: Harper and Brothers, 1942, p. 59.

<sup>13</sup> M. T. Florynsky, *Toward an Understanding of the USSR*, p. 198.

<sup>14</sup> A. R. Williams, *The Soviets*, p. 173. Reprinted by permission of the publishers.

<sup>15</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 59.

types of equipment, and were the first to be given selected seeds and artificial fertilizers As the state farms increased in number from 1400 in 1928 to well over 4000 in 1934, and as the quantity of cultivated land at their disposal increased from 17 to 16 million hectares, many people concluded that the Soviet leaders intended to convert all Russian agriculture into state farms sooner or later and that the collective farms were merely being tolerated as a transitional form of organization

This conclusion was unwarranted To be sure, the state farms achieved great increases in total physical output, in value-product, and in the output per work-day or work-hour, and before the war they produced some 10 per cent of the total grain crop and 15 to 20 per cent of the marketed grain<sup>16</sup> On the other hand, the state farms incurred the severe displeasure of the Soviet leaders They operated at a loss year after year, in the sense that they exceeded their budget estimates of cost while actual income fell short of budget figures They were criticized for cultivating only a small fraction of their total area of 84 2 million hectares They were badly managed in part because of slackness or dishonesty of the management and in part because they were too large to be managed effectively by anyone Labor and management turnover was great, personnel costs were high, and livestock mortality was excessive Far too great a proportion of their products was consumed on the state farms themselves so that relatively little was available for the market, and there was much theft and waste in production As a result of these difficulties, many state farms were liquidated between 1934 and 1937, the size of the survivors was reduced, the total land at their disposal decreased from 84 2 to 60 3 million hectares, and their cultivated area declined from 16 to 12 4 million hectares<sup>17</sup> Since these readjustments the surviving state farms have functioned in much better fashion, but the collective farms are likely to remain for a long time as the mainstay of Russian agriculture

*The Organization of the Collective Farms* As of the beginning of 1947, there were 220,000 collective farms in the U S S R<sup>18</sup> On the basis of their total cultivated area in the prewar period, their average size would be 533 hectares, or 1316 acres, of cultivated land Their average size before the war was estimated to be 1198

<sup>16</sup> *Ibid.*, p. 60

<sup>17</sup> A. Buzkov, *The Development of the Soviet Economic System*, pp. 332-333

<sup>18</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 51

acres.<sup>19</sup> They included 93.5 per cent of all the peasant households of the country and averaged about 75 households per farm. Membership in the collective farms was open to all citizens 16 years of age or over. There was an admission fee of 20 to 40 rubles, and the applicant for membership had to contribute his property to the collective farm, with one-fourth to one-half of it going into the so-called indivisible fund of the collective farm so that it could not be returned to the incoming member if he later decided to withdraw.<sup>20</sup>

The land used by the collective farms belongs to the people of the nation as a whole through the government, but the collective farms have been granted "perpetual use" of their land. There is collective or cooperative property in the common farm buildings, draft animals, some livestock, tools and implements of production, and stocks of seed. The individual collective farmers are allowed the use of small plots of land (varying from one-fourth to one hectare) for their own purposes. They may own their homes and small quantities of livestock (including cattle, pigs, sheep, goats, poultry, rabbits, and bees). The heavy farm machinery such as tractors, trucks, harvesters, combines, and the like, are owned neither by the collective farmers nor directly by the government. Instead, the machinery is owned by separate government-controlled agencies known as Machine Tractor Stations. There were only 158 of these stations in 1930, but the number grew to 6980 in 1940 and was no less than 7584 as of the beginning of 1947.<sup>21</sup> The collective farms must make use of these Machine Tractor Stations and their services (if available), and make payment in kind or in cash.

The operation of each collective farm is nominally quite democratic. That is, the general assembly of collective farmers on each farm elects a president, executive board, and a control committee. The latter agency supervises the acts of the officers and attempts to insure plan fulfillment. Cultivation of the land is carried on by brigades composed of 40 to 60 workers and the "brigadiers" or brigade commanders assign the workers to their tasks. The collective farmers are really farmers and not merely governmental employees, so their income depends directly upon the crops which they pro-

<sup>19</sup> *Communism in Action*, p. 73.

<sup>20</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, p. 205.

<sup>21</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 331, and Harry Schwartz, *Russia's Postwar Economy*, p. 55.

duce After certain deductions (to be described later) are made from the harvest, the remainder is distributed in kind among the collective farmers or is sold for cash, which is then distributed The collective farmers do not share equally in the available income, but are paid on the basis of "labor days" The labor day is an abstract unit supposedly based on such factors as skill, social usefulness, and physical exertion The individual collective farmers receive credit for from one-half to two labor days for each day's work There are also premiums and deductions for over-accomplishment and under-accomplishment The share of an individual farmer is, then, determined by the number of days he works multiplied by the labor-day multiple for his type of work, divided by the total number of labor days contributed by all members of the collective farm, multiplied by the amount of product or cash available for distribution

*Compulsory Deliveries of Agricultural Products* Among the deductions which are made from the harvest before there can be a net amount to sell for cash on the market or distribute in kind among the collective farmers, the most important deductions are the compulsory deliveries to the government The compulsory delivery of any crop is that proportion of the collective farm's output that must be sold to the government at a price which is arbitrarily set far below the market value of the product The compulsory delivery is sometimes regarded as a tax on agricultural production, on the ground that the same result is achieved by taking a portion of farm produce at an arbitrarily low price as would be achieved by letting the farmers sell their crops for full market value and then taking a portion of their income by means of taxation On the other hand, some people regard the compulsory delivery as a rent which is paid to the government for the private (cooperative) use of publicly owned land

The compulsory deliveries amounted to 15 per cent of the gross yield of grain and leguminous plant crops for all collective farms in the U.S.S.R. in 1938<sup>22</sup> Similar levies were made on other products of the collective farms, for the compulsory deliveries apply not only to grains but also to technical crops (such as cotton, flax, and sugar beets) and to meat, potatoes, wool, milk, and other things Thus, at one time the government was taking all potatoes up to 22 quintals per hectare, all wool up to 44 pounds per sheep, and

<sup>22</sup> *Ibid.*, p. 311

all milk up to 48 gallons per cow<sup>23</sup> The size of the compulsory deliveries varies greatly from one crop to another In 1938, for example, 90 per cent of the cotton grown on non-irrigated land went to the government in compulsory deliveries<sup>24</sup> The compulsory deliveries are 5 to 10 per cent higher for individual peasant farmers than for collective farmers, and higher also for collective farms which are not served by Machine Tractor Stations than for those which are so served The latter provision does not indicate, as some critics allege, that the farms without Machine Tractor Station services are more efficient and productive than the others It indicates merely that the government is not so completely dependent upon the compulsory deliveries alone for its grain collections when the farms are served by Machine Tractor Stations for whose services a charge may be made Finally, the compulsory deliveries apply even to the farm produce which the individual collective farmers raise on their own small farmsteads

Prior to 1933, the compulsory deliveries were based on "contracts" between the government and the peasant or collective farmers, though the farmers had no control over quantities to be delivered or prices to be received Sometimes the contracts called for a definite proportion of the gross crop, while in other cases they specified minimum amounts per hectare and the remainder of the marketable surplus The demands of the government were subject to arbitrary change, and the deficiencies of some farms were sometimes collected from other farms The system was changed to one of "fixed deliveries" in 1933 That is, the farmers had to deliver so much product per hectare of cultivated land or other unit of measurement This meant, of course, that if a collective farm increased its output by bringing more land under cultivation, the total amount deliverable to the government increased In 1940, the system of compulsory deliveries was changed again, so that they are based on the total areas of the collective farms instead of the areas cultivated according to plan This may operate to give incentives to the collective farmers, since any increase in output, whether obtained by bringing more land into use or by other methods, will not affect the total quantity to be delivered to the government On the other hand, if the collective farms have much land which is unsuited to cultivation, the new levies based on total area may become almost im-

<sup>23</sup> N de Basily, *Russia under Soviet Rule*, p 335

<sup>24</sup> A Baykov, *The Development of the Soviet Economic System*, p 312

possible burdens on the actual cultivated land. Not only are the compulsory deliveries rather heavy, but also the prices paid for such deliveries are very low. In general, they probably do not run over 20 per cent of the market prices of the products.

**Other Deductions** After the compulsory deliveries have been made, the harvest of a particular crop is subject to other deductions. Collective farms served by Machine Tractor Stations must pay for the services received. These payments, made in cash or kind, run fairly large. In 1938, for example, they took 16 per cent of the gross yield of grain and leguminous plant crops for all collective farms in the U.S.S.R.<sup>25</sup> The collective farmers must make other payments to the government on account of the interest or principal of loans received in the past from the appropriate governmental credit agencies. They must pay a milling tax to the government when they get grain processed for their own use. This tax may run as high as 10 per cent of the grain so milled. After all these deductions have been made, the collective farms are required by law to put aside funds for seed reserves, seeds for the current year, fodder, mutual aid, relief in emergencies, and insurance. In the end, the amount of the gross harvest available as income to the individual members of the collective farms has been estimated to run not over 35 to 39 per cent, and was actually 32 per cent in the case of grain and leguminous plant crops for all collective farms in 1938.<sup>26</sup>

**Voluntary Deliveries** The net amount of the harvest available to the collective farmers is also sold to the government in the case of the technical crops (cotton, flax, sugar beets, and other things). In the case of other products, the collective farmers have a choice of selling the remainder of the harvest to the government or of selling it on the open market. Such sales to the government are called voluntary deliveries. The basic prices for voluntary deliveries are about 25 per cent higher than those for compulsory deliveries. Moreover, there are premiums above the basic prices for voluntary deliveries of large quantities of produce. A collective farm which voluntarily delivers 10 to 50 quintals of grain to the government gets a premium of 10 per cent above the basic price, while one whose voluntary delivery reaches 1000 quintals receives double the

<sup>25</sup> *Ibid.*, p. 311.

<sup>26</sup> *Ibid.*, and A. Yugow, *Russia's Economic Front for War and Peace*, p. 65.

basic price<sup>27</sup> An attempt has also been made to increase voluntary deliveries by means of a "stimulation fund" This means that co-operative stores in the country have certain articles on hand which can be obtained only as a reward or premium for selling specified quantities of farm produce voluntarily to the government These articles either cannot be obtained at all by any other method or can be obtained only with great difficulty and delay On the whole, however, since the prices paid for voluntary deliveries, even with the premiums added in, are still below the market prices for farm products, the system of voluntary deliveries has been none too successful.

**Collective Farm Peasant Markets** The alternative to voluntary deliveries is the sale of the net produce of the collective farms (or of the individual collective farmers, or of individual peasant farmers) on what are called collective farm peasant markets These are merely open spaces with tables or booths which are hired by the farmers In conjunction with them, the state may operate stores selling manufactured goods, so the farmers will have a chance to spend their money at once, or stores selling farm products, in order to keep prices in the farm markets in line with governmental price policies The produce sold in the farm markets comes only from the immediate local areas, but the farmers a few years ago were getting a fourth of their money income from sales in these markets Of the produce sold in them, collective farms as such furnished only 15 per cent, individual members of collective farms provided 75 per cent (two-fifths from their individual homesteads and three-fifths from their shares of collective produce received on the basis of labor days), and the individual peasant farmers furnished 10 per cent<sup>28</sup> Only private individuals may buy in these markets The prices received by the farmers approximate those in the governmental (commercial) stores, but are well above those for compulsory or voluntary deliveries Thus, we see that the net amount of collective farm produce, after all deductions, may be distributed to the collective farmers on the basis of labor days, so the farmers may sell it by voluntary deliveries or on the market, or the net produce may be sold directly by voluntary deliveries or on the market and the cash distributed to the farmers on the basis of labor days The net produce of individual peasant farmers or that

<sup>27</sup> F Utley, *The Dream We Lost*, p 155

<sup>28</sup> L E Hubbard, *Soviet Trade and Distribution*, p 146

raised by collective farmers on their own homesteads may be sold also by voluntary deliveries or on the farm markets

*The Control of Collective Farming.* Since the main part of Russian agriculture is operated by collective farmers and not directly by the government, the question is raised sometimes as to how the economic planners can make plans for agriculture and be sure that these plans will be carried out. The answer to this question is relatively simple. By applying discriminatory compulsory deliveries to various crops or by varying the prices at which the compulsory deliveries are taken, the government can encourage the production of some crops and discourage that of others. The government can refuse the services of Machine Tractor Stations to collective farms which raise the "wrong" crops, or it can make higher charges for the services of these stations. It can refuse loans or charge high interest rates to farms which wander from the path of rectitude. It can alter the prices at which voluntary deliveries of various crops are taken and can control the prices which prevail on farm markets. It can vary the kinds, quantities, qualities, and prices of consumers' goods available for the farmers in the retail stores of the rural areas. Surely, if the Russian farmers remain blessed with any economic motivation, the government can achieve a great measure of control over their agricultural activities by these means. The farmers are also subject to direct political control. The government issues laws and decrees, supported by heavy penalties, which are binding on all collective farmers. Moreover, each Machine Tractor Station has two staffs which assist the director. One is composed of engineers, mechanics, and agronomists, while the other staff is a policy section of the Communist Party which is responsible for the political education of the farmers and the liquidation of enemies of the regime. The policy section sees to it that everyone does his duty, directs grain and other deliveries to the government, sums up accomplishments and failures, analyzes problems, and gives instructions for future production to the farmers. There can be little doubt that the Russian government is able to control collective agriculture.

*Collectivization and Mechanization of Agriculture.* In discussing the results of agricultural operations in the Russian planned economy, we may say that at least two of the goals of the planners have been achieved in large measure. Earlier in the chapter we noted that the Russian leaders have reached their goal of taking agriculture almost completely out of the hands of individual peasant

farmers and that, under the pressure of various circumstances, this collectivization occurred much more rapidly than had been expected. A second goal which may be regarded as fulfilled is that of the mechanization of Russian agriculture. In 1927, Russia had about 25,000 tractors, all of foreign origin, but by 1941 the number had grown to 547,000 and they had been made in Russia. In 1927, there were virtually no combines in Russian agriculture. In 1939, there were 125,000 and in 1940, 182,000. In 1930 the Machine Tractor Stations cultivated 1,200,000 hectares of land while in 1938 they served 66,000,000 hectares.<sup>29</sup>

On the other hand, both of these results or achievements are open to serious criticism. The process of collectivization was extremely brutal and costly in terms of human lives and suffering, and the actual productive results of collectivized agriculture have all too often fallen far short of expectations. Tractors, combines, and other agricultural machines have increased in number in amazing fashion, but mere quantity figures tell us nothing about the quality of the machines or their susceptibility to breakdown and do not indicate whether the machines were produced at reasonable or exorbitant cost. It may be, as some critics alleged, that the Soviet economy rushed madly along for some years in the production of agricultural machinery without taking the trouble to produce adequate supplies of repair parts or to train adequate numbers of machine operators, mechanics, and repair men. Again, it has been stated definitely that the increase in the number of tractors under the First Five-Year Plan, especially in view of the inexperience in their use, could not make up for the losses in draught animals (horses and oxen).<sup>30</sup> At all events, it is necessary to admit that the mechanization of Russian agriculture was slow to show tangible results in the form of increased agricultural production.

*Results of Russian Agricultural Production to 1940.* In Table 7, we present some of the important results of agricultural operations in Soviet Russia in selected years before World War II in comparison with planned estimates. There is no doubt that the results were disastrous under the First Five-Year Plan. Grain and flax production were already smaller in 1928 than in 1913, while the sugar beet crop was about the same size as in 1913, and there were considerable declines in grain and sugar beet production from

<sup>29</sup> A. Yugow, *Russia's Economic Front for War and Peace*, pp. 54-55.

<sup>30</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 202.

1928 to 1932 The total land in cultivation increased by about 19 per cent from 1928 to 1932, but the production of all the leading crops in 1932 was far short of planned estimates Actual production as a percentage of planned production was 66 for grains, 66 for cotton, 81 for flax, and 39 for sugar beets During the 1928-32 period the land devoted to grain production increased by 75 million hectares, but average yield per hectare was badly off and the 1932 grain crop was 13 per cent smaller than the 1913 crop <sup>31</sup> The land devoted to technical crops increased from 4.6 million hectares in 1913 to 8.6 in 1928 and 11.9 in 1932, but the yield per hectare of these crops from 1930 to 1933 averaged only a little over 50 per cent of the yields obtained before World War I <sup>32</sup>

The unfavorable showing made by the leading crops in 1932 was the result of many factors The land in cultivation had been increased rapidly, and it outran the ability of the farmers and their tractors and draught animals to give it good cultivation The management of collective farms was inefficient and subject to frequent changes, and there was a shortage of workers of certain kinds, especially machine operators Much of the farm work was done in common, and remuneration per household was more likely to be on the basis of the number of mouths to be fed than on the basis of the quality and quantity of work performed Land was still being reassigned among the collective farms Plans for state procurements of agricultural products were not yet accurately determined or known in advance, and the collective farmers were uncertain as to what they might expect to get for their labors With crops rather small, government requisitions actually took large proportions of them and left very little for the farmers Finally, it was still uncertain as to whether the private production of the individual collective farmer was lawful and to what extent, if any, he had a right to dispose of it on the market <sup>33</sup>

The production of these leading crops made noteworthy progress during the period of the Second Five-Year Plan In all cases, production in 1937 was far above the 1932 level, and that for grains and cotton actually exceeded the planned estimates by considerable amounts The 1937 results may be discounted in several ways, however In the first place, 1937 was one of the best crop years in

<sup>31</sup> *Ibid.*, p. 325

<sup>32</sup> B. Butzkus, *Economic Planning in Soviet Russia*, p. 209

<sup>33</sup> A. Baykov, *The Development of the Soviet Economic System*, pp. 202-204

Russian history and it is uncertain how much credit for the large crop should be given to favorable growing conditions and how much to Russian agricultural organization, methods, and efforts Again, we are told that statistics for Russian crops since 1933 are quoted in terms of "biological yield" rather than actual yield The biological yield is the amount of the crop standing in the fields minus an arbitrary deduction of 10 per cent for loss in harvesting It is claimed that, since the actual loss in harvesting has run as high as 40 per cent of the crop in some cases, the figures for biological yield seriously overstate the amount of the crop actually realized<sup>44</sup> Finally, quite a large part of the increases in crop yields seems to be due to increases in the quantity of land under cultivation rather than to increases in the yield per hectare of land Under modern mechanized methods of production, it would be logical to expect heavily increased yields per hectare, but the actual yields per hectare for some important crops were less in 1937 than in 1913 The total outputs of important crops in 1940 were greater in some cases and smaller in others than those for 1937, but, in all cases, much further progress had to be made in order to reach the planned goals for 1942

The results of livestock production in Soviet agriculture were particularly unsatisfactory under the First Five-Year Plan The total numbers of the kinds of livestock considered in Table 7 dropped from 276 7 to 124 0 million head—a decline of about 55 per cent, although the plans called for an increase of over 13 per cent The quantity of livestock on hand in 1932, as a percentage of

<sup>44</sup> F Utley, *The Dream We Lost*, p 156

TABLE 7  
RESULTS OF SOVIET RUSSIAN AGRICULTURAL OPERATIONS IN

Item	Unit	1913	1928
1 Land under cultivation	Million hectares	105 0	113 0
2 All grains, total production	Million metric quintals	801	733
3 Cotton, total production	Million metric quintals	6 8	8 2
4 Flax, total production	Million metric quintals	5 1	3 2
5 Sugar beets, total production	Million metric quintals	99 2	101 4
6 Horses on hand	Million head	35 8 <sup>a</sup>	33 5
7 Cattle on hand	Million head	60 6 <sup>a</sup>	70 5
8 Sheep and goats on hand	Million head	121 2 <sup>a</sup>	146 7
Pigs on hand	Million head	20 9 <sup>a</sup>	26 0

<sup>a</sup> 1916 Result.

planned estimates, was 53 for horses, 50 for cattle, 32 for sheep and goats, and 33 for pigs. The main causes of the reduction in livestock were the great slaughter of farm animals by the well-to do farmers during the anti-kulak campaign and by the smaller peasants in resistance to collectivization, poor care of livestock and a shortage of buildings for livestock on the newly collectivized farms, the low level of grain production during the period, and uncertainty concerning state requisitions and the ability of individual collective farmers to own livestock.<sup>25</sup> After 1932, livestock production made considerable progress, but in 1940 the quantities of livestock on hand were below both the 1928 and 1916 levels for three of the four important categories.

*Evaluation of the Collective Farms* A number of features of the organization and operation of the collective farms came in for severe criticism in the years before World War II. In the first place, it was often contended that the collective farms were cooperative in name only. Actually, the leading officials and managers were usually Communists nominated by local Soviets or local units of the Communist Party. Governmental decrees and orders affecting the collective farms were binding on all collective farmers and went into effect without even any preliminary discussion by the farmers. The administration of the collective farms by the Communists was said to be high-handed and arbitrary, and many complaints were made about the exclusion or ejection of collective farm members without adequate reason and without the necessary two-thirds vote.

<sup>25</sup> A Baykov, *The Development of the Soviet Economic System*, pp. 200-201.

TABLE 7 (continued)

SELECTED YEARS, IN COMPARISON WITH PLANNED ESTIMATES

1932 (actual)	1932 (planned)	1937 (actual)	1937 (planned)	1940 (actual)	1942 (planned)
134 4	141 3	135 3	139 7	151 0	157 0
699	1058	1203	1048	1190	1300
12 7	19 1	25 8	21 2	25 2	32 9
5 0	6 2	5 7	8 0	6 7	8 5
65 6	195 5	218 6	276 0	222 0	282 0
19 6	36 9	16 7	21 8	20 5	21 9
40 7	80 9	57 0	65 5	56 0	79 8
52 1	160 9	81 3	96 0	93 0	170 7
11 6	34 8	22 8	43 4	28 0	45 6

of the members<sup>36</sup> This problem was recognized finally by the government in 1938 and a decree was issued forbidding purging, the exclusion of members because they are also employed in state enterprises, and exclusion because of the breaking of the internal rules of the collective farms. In the future, exclusions were to be based entirely on rules laid down from above and were to be ratified by the executive committee of the district<sup>37</sup>

The criticism that the collective farms are not truly cooperative sometimes takes a different turn and it is alleged that the collective farms really operate by means of private peasant farming. Since 1934, the individual collective farm members have had a right to small homesteads of their own, varying in size from one-fourth to one hectare, on which they can raise crops and livestock. It is said that the farmers began immediately to work hard on their own land and let things slide on the collective land, with the result that yields per hectare were high on the individual homesteads and low for the collective land. By 1938, the individual farmsteads were said to account for almost half the cattle, pigs, sheep, and goats on hand and for 21.5 per cent of gross agricultural production<sup>38</sup>. These results seemed amazing in view of the fact that the cultivated land in the individual homesteads amounted officially to only 3.9 per cent of the total cultivated area of the country.

The real explanation of these results was found in the fact that the managers of the collective farms, in despair over the prospects of increasing truly collective production, had been illegally turning over large quantities of collective land to the individual farm members for private cultivation in the hope that in this way it would be possible to fulfill the plans for agriculture. The Soviet leaders, of course, knew of this development, and by 1939 they apparently thought that the position of agriculture was strong enough so that they could begin a drive to get the collective land back from the individual collective farm members and socialize their livestock as well. By a famous decree of May, 1939, new limitations were placed on the size of the farmsteads held by individual members of collective farms, on the amounts of livestock they could own, and on their rights to fodder and pasture<sup>39</sup>. The individual homesteads

<sup>36</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, pp. 210-211.

<sup>37</sup> *Russian Economic Notes*, Number 368, pp. 1-2.

<sup>38</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 327.

<sup>39</sup> Decree of the Central Committee of the Communist Party, May 27, 1939.

were to be as small as one-tenth of a hectare in some cases, and a special corps of inspectors was given the duty of seeing that collective land was not improperly turned over to the individual collective farmers. Each collective farmer was henceforth required to spend at least 80 days per year on the average in working on the collective farm land, or face expulsion. Since 80 days per year are not over a fourth of the available working days, we may say that, if the collective farm members formerly spent fewer days on the collective land, either they did very little work altogether or else collective farming actually operated almost entirely on the basis of private farming.

Another decree based the compulsory deliveries of meat for collective farms on the total areas of these farms rather than on the number of collective farm animals. Fulfillment of the levies required the collective farms to purchase a large part of the livestock of the individual members. These purchases could be made at the state prices for livestock which ran far below the actual market values. Finally, a decree placed new burdens on the individual farmers. It required that taxes and other deliveries must be rigorously collected, reinstated the former heavy tax on horses, and provided road work, timber cutting, and other unpleasant pursuits for any infractorious farmers.<sup>40</sup>

The distribution of income on the collective farms has been criticized severely. For example, an equal distribution of collective farm income would have been more suitable than distribution on the basis of labor days. Equal division would have been simple, in line with certain former practices of the peasants, and a good method of sharing inadequate supplies. The labor-day system is complicated, cumbersome, and difficult to apply in agriculture. However, an equal division of income would have still further reduced the labor incentives of the farmers, and it is often held that these have been inadequate under the labor-day system. Since the collective farmers are paid on the basis of labor days worked, they have been sorely tempted just to put in their time. By merely going through the motions, they could get paid as much as individuals who put forth great efforts, and the industry of one man can be easily offset by the laziness of another. Moreover, it has been alleged that the labor days credited to the individual collective

<sup>40</sup> *Russian Economic Notes*, Number 368, pp. 36

farmer were more likely to depend on the good will or ill will of the farm officials than on anything else.<sup>41</sup>

There is little doubt that the Russian leaders have had a difficult problem in furnishing incentives to the collective farmers. In the first place, severe penalties have been provided for the recalcitrant farmers. Reprimands, fines, demotions, suspensions, and expulsions are provided for laxity, negligence, or refusal to work, and, if the farmers' sins involve "counter-revolutionary activities" or "crimes against socialist property" (such as stealing food from collective lands), long imprisonment or death may be the result.<sup>42</sup> Another attempt to deal with the problem of incentives was found in the decree which based compulsory deliveries of farm produce on the total areas of collective farms, thus giving the farmers every reason to expand output and bring unused land under cultivation.

Again, in 1938, the Russian leaders officially noted widespread improper uses of collective farm income. Too much income was being devoted to the construction of community buildings, to administrative expenditures, and to actual production expenses. Officials of collective farms were drawing up their budgets without consulting the members or were disregarding budgets that had been properly drawn up. A decree was issued providing that capital investments should not use up over 10 per cent of collective farm cash incomes, that no more than 70 per cent of budgeted operating expenses should be paid before the results of the harvest were known, and that the individual farm members should have at least 60 per cent of the cash income distributed among them.<sup>43</sup> A 1939 decree then provided that the collective farms should pay taxes, insurance, and loans to the state, pay current expenses of production, pay administrative expenses (not over 2 per cent of total income), assign funds for cultural needs, replenish indivisible funds (by 12 to 15 per cent of income on grain farms and by 15 to 20 per cent on farms raising technical crops and livestock), and divide the entire remainder among the members.

A further attack on the problem of incentives was made in 1940 when a decree was issued providing premiums and bonuses for improvements in the quality or quantity of farm production made by individual members of the collective farms or others. For ex-

<sup>41</sup> F. Utley, *The Dream We Lost*, p. 155.

<sup>42</sup> M. T. Ilorinsky, *Toward an Understanding of the USSR*, p. 203.

<sup>43</sup> *Russian Economic Notes*, Number 368, pp. 3-4.

ample, "a milk maid receives 15 per cent of the milk above her assigned milking task, the dairymaid who tends to the calves receives one-half kilogram of meat for each 10 kilograms' gain in weight per head above the plan, hog breeders receive every fifth suckling pig above the plan, poultry raisers receive 15 per cent of the eggs and 50 per cent of the chicks above the norm, and so on"<sup>44</sup> However, the extra rewards were also given to brigade leaders, farm presidents and other officials, agronomists, veterinarians, technicians, engineers, teachers, and doctors, and it is possible that the new system of bonuses really favored the bureaucracy of the collective farms and not the individual farmers. The bonuses were small for individual farmers, but the officials and technicians might get a bonus of one to three months' salary for fulfillment or over-fulfillment and were expected to drive the individual farmers who were really forced workers. That a problem of incentives also existed in the Machine Tractor Stations is indicated by the fact that, in 1940, a decree was issued forbidding the willful abandonment of work by tractor drivers and combine operators, subject to all the penalties applied to industrial workers. The penalties could include two to four months in prison or six months of correctional work on the regular jobs at a 25 per cent reduction in pay.

*The Status of the Russian Farmer* In considering the economic status of the farmer in Soviet Russia in the years before World War II, we shall be primarily concerned with the collective farmers. We have already noted that the workers on the state farms were treated very well on the whole, since they had numerous personal privileges and received wages which compared favorably with those of industrial workers. It is not at all difficult to find unfavorable estimates of the lot of the collective farmers. In the matter of prices, it was said that, during the famine of 1932, the price of grain was only 75 per cent higher than in 1913, though the prices of manufactured goods were about five times higher than in 1913. In the next few years, agricultural prices rose by 25 to 50 per cent but those of manufactured goods went up several hundred per cent.<sup>45</sup> In 1936, one pood of rye flour (36.11 pounds) would purchase one-half kilogram of sugar, 1.3 kilograms of soap, one-half meter of

<sup>44</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 77. Reprinted by permission of Harper and Brothers, New York.

<sup>45</sup> F. Utley, *The Dream We Lost*, pp. 150-151.

leather boots. In 1913, the same quantity of rye flour would have purchased 41 kilograms of sugar, 33 kilograms of soap, 64 meters of cotton cloth, 270 liters of kerosene, or one-seventh of a pair of leather boots.<sup>46</sup> Apparently the famous "scissors problem" was still something of a bogey for the Russian farmers.

The average money income of able-bodied collective farmers in 1935 was not over 350 rubles, as compared with an average wage of 2270 rubles in industry.<sup>47</sup> In 1939, the average money income of the collective farmer was 982 rubles, while the average wage in industry had passed the 3500 ruble level.<sup>48</sup> Of course, there were great variations in income from one collective farm to another. In 1937, there were 610 collective farms with a money income of more than a million rubles each, whereas the average farm had a money income of only 60,000 rubles, and some of the poorer farms, only 1000 to 5000 rubles.<sup>49</sup> Allotments of grain per labor day varied between one and a half kilograms or less and 15 kilograms or more, and the cash income per labor day varied from less than one ruble to more than three rubles.<sup>50</sup> Since the really prosperous collective farms are only a fraction of one per cent of the total number while their large incomes raise the average incomes of all collective farms quite a little, it follows that most collective farmers were not as well off as the figures for average income would indicate.

In considering the actual goods available for the farmers, it was pointed out that the rural population was between two and three times as numerous as the rest of the population, while the manufactured goods allotted to the stores in rural areas amounted only to about 35 per cent of the total value of industrial goods distributed through retail trade.<sup>51</sup> Even counting purchases by farmers in the urban stores, it is clear that the farmers got much less than their proportionate share of these products. On the other hand, the agricultural population was said to have less to eat than before the revolution. In 1938, some 40 per cent of the total grain crop reached the market as compared with 26 per cent in Tsarist times, though the crop of 1938 was only slightly larger than that of 1913. Again,

<sup>46</sup> L. E. Hubbard, *Soviet Trade and Distribution*, p. 290.

<sup>47</sup> *Ibid.*, p. 298.

<sup>48</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 68.

<sup>49</sup> *Ibid.*, p. 67.

<sup>50</sup> *Ibid.*, pp. 69-70.

<sup>51</sup> L. E. Hubbard, *Soviet Trade and Distribution*, pp. 289-290.

state grain collections in 1937 were 150 per cent larger than in 1928 though the harvest was only 50 per cent greater, which indicates that the state share of the crop increased by about two thirds between these two years.<sup>52</sup> Thus, it was claimed that the government takes more in taxes (compulsory deliveries) than the peasants lost formerly because of rent and interest. Agriculture, however, is the chief support of Russian industry and the mainstay of the economy as a whole. The large funds for capital investment in industry are derived to a great extent from a turnover tax, and the turnover tax on foods and agricultural products in general has in some years yielded four times as much revenue as the turnover tax on industrial products. Thus, the turnover tax on agricultural products, which makes up all or most of the differences between the prices received by farmers and the prices which these products command on the market, in effect placed a large part of the burden of industrialization on the agricultural industry.

On the basis of these considerations, it is possible to conclude that, in the change from capitalism to socialism, the Russian farmers merely exchanged one oppressive master for another, that the farmers were actually worse off in the modern socialized economy than they were in Tsarist days, and that the farmers were exploited severely in order to create the manufacturing industries which, according to this point of view, are only expensive toys. Certainly, the development of Russian agriculture in the socialized economy was much less successful and satisfactory than that of industry, and it furnished one of the most serious problems, if not the most serious, which the economic planners had to face.

On the other hand, it is very difficult to get accurate information on prices, incomes, and standards of living in Soviet Russia, and, if the claims of the Russian government with respect to the total income received from all sources by the average collective farmer are at all valid, the Russian farmer is not badly off in comparison with the average industrial worker. For example, Soviet authorities stated that the average personal income of the collective farmer from all sources amounted to 5843 rubles in 1938, as compared with 2132 rubles in 1928.<sup>53</sup> The lot of the farmers was also improved by a great increase in educational facilities, public libraries, clubs,

<sup>52</sup> F. Utley, *The Dream We Lost*, p. 152.

<sup>53</sup> *Russian Economic Notes*, Number 20, pp. 25.

theaters and cinemas, newspapers, doctors, and hospitals, maternity homes, and nurseries<sup>54</sup>

Collectivized agriculture in the years before the war had begun to show some of the productive results which were expected of it in earlier times, and the prospects were rather encouraging. In spite of all difficulties, Russia under socialism led the world in the production of wheat, rye, barley, oats, flax, potatoes, sugar beets, and other farm products, and developed many "new" products, such as tea, mandarins, lemons, grapefruit, oranges, tobacco, camphor, geranium, grapes, eucalyptus, oleander, four kinds of rubber-producing plants, southern hemp, soybeans, kenaf, and castor beans.<sup>55</sup> Finally, in view of the ability of the Russian armed forces to stand up before the onslaught of Nazi Germany, it is necessary to believe that the Russian manufacturing industries, obtained at the cost of heavy sacrifices on the part of agriculture, were something much more efficient and useful than the term "expensive toys" would indicate. It appeared that the Russian economy really got something in return for the sacrifices and hardships incidental to industrialization.

*Russian Agriculture in Wartime* Russian agriculture, like Russian industry, suffered severe losses during World War II. The area occupied by the Germans contained about 40 per cent of the total cultivated land of the country and had formerly produced 45 per cent of the country's wheat, 41 per cent of the rye, and large amounts of sugar beets, flax, hogs, and other farm products.<sup>56</sup> During the war 98,000 collective farms, 1876 state farms, and 2890 Machine Tractor Stations were ruined.<sup>57</sup> Other losses included 137,000 tractors, 49,000 combines, 4 million plows and harrows, over a million seeders and threshers, 7 million horses, 17 million cattle, 20 million hogs, 27 million sheep and goats, and 110 million poultry.<sup>58</sup>

War losses of acreage were replaced to some extent as some 3½ million acres were brought into use in Siberia, 2½ million acres were cultivated through factory auxiliary-farms, another 2½ million acres of victory gardens were cultivated by 10 million people, and

<sup>54</sup> A. Brykov, *The Development of the Soviet Economic System*, p. 328.

<sup>55</sup> *Foreign Commerce Weekly*, March 1, 1941, pp. 362-363.

<sup>56</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 7; E. Snow, *People on Our Side*, pp. 69-70; M. Dobb, *Soviet Planning and Labor in Peace and War*, pp. 101-102.

<sup>57</sup> Harry Schwartz, *op. cit.*, p. 16.

<sup>58</sup> *International Conciliation*, April, 1948, p. 265.

some 20 million acres were brought into use by collective and state farms which had not been over-run by the invaders Working days per individual on the collective farms were stepped up sharply to a minimum of 150 per year By 1913, some 70 per cent of all agricultural workers were women, and a million more women were in training to handle heavy machinery<sup>59</sup>

In spite of everything, however, Soviet Russian agricultural production was at low ebb during the war Most of the able-bodied farm workers had gone to war and the army had taken many of the tractors and horses The remaining machinery deteriorated rapidly as it was over-utilized by relatively unskilled workers who were short of repair parts and mechanical knowledge The increases in acreage noted above were canceled in large part by a lowered quality of cultivation that allowed the fields to become choked with weeds An almost complete lack of artificial fertilizer and insecticides was another unfavorable factor As a result, in spite of the fact that it was about the best crop year since the beginning of the war, agricultural production in 1915 was only about half that of 1910<sup>60</sup>

Familiar types of abuses were apparently present in the operation of collective farms during the war period Income was mis-distributed, with shares going to village officials, barbers, lazy farmers, and surplus administrative personnel After the war, some 600,000 individuals were stricken from the payrolls or put to work at tasks more closely connected with the raising of crops In the second place, there was again widespread misappropriation of collective farm land by private individuals and enterprises Postwar measurements found 2,224,000 cases of illegal occupancy of collective farm land and returned 47 million hectares to the collective farms Third, collective farm officials had violated farmers' rights to choose their own officials, to express their views as to how the farms should be run, and to check the collective farm accounts Finally, Communist Party officials, state agencies, and farm officers, had stolen food, livestock, feed, and money from the collective farms or had taken these things with very little returns to the farmers After investigation, 150,000 livestock and 15 million rubles were restored to the collective farms<sup>61</sup>

<sup>59</sup> L. Snow, *People on Our Side*, pp 108-110

<sup>60</sup> Harry Schwartz, *Russia's Postwar Economy*, p 54

<sup>61</sup> *Ibid.*, pp 55-57

*Russian Agriculture Under the Fourth Five-Year Plan* In Table 8, we present data on several important phases of Soviet Russian agriculture, showing their status in 1945 in comparison with 1910 and with 1942 plans, the goals set up for 1950 under the Fourth Five-Year Plan, and, in some cases, the progress which had been made by 1947 While the goals of the Fourth Five-Year Plan are in almost all cases in excess of the actual results for 1940, they uniformly fall short of the goals which had already been set up for

TABLE 8

*RESULTS OF SOVIET RUSSIAN AGRICULTURAL OPERATIONS IN 1910  
1945, AND 1947, IN COMPARISON WITH PLANNED ESTIMATES FOR  
1942 AND 1950*

Item	Unit	1940 (actual)	1942 (planned)	1945 (actual)	1947 (actual)	1950 (planned)
1 All grains, total production	Million metric tons	119.0	130.0	66.5	96.5	127.0
2 Cotton, total production	Million metric tons	2.7	3.3	1.2	1.9	3.1
3 Sugar beets, total production	Million metric tons	20.9	28.2	8.9	15.7	26.0
4 Sunflower seed, total production	Million metric tons	3.3		1.8	2.5	3.7
5 Horses on hand	Million head	20.5	21.9	10.5		15.3
6 Cattle on hand	Million head	56.0	79.8	46.9		65.3
7 Sheep and goats on hand	Million head	93.0	170.7	69.4		121.5
8 Pigs on hand	Million head	28.0	45.6	10.4		31.2

1942 However, in view of the very low levels which prevailed actually in 1945, the 1950 goals will call for tremendous efforts on the part of all concerned if they are to be achieved

Unfortunately for hopes in this direction, 1946 was a year of miserable crop failure in the U S S R The chief cause was a great drought, which was said to have been the worst in 50 years Other causes of lesser importance were continued careless and low quality work by many groups of farmers, a scarcity of skilled agricultural specialists, the shortage of draught power and farm machinery, and the poor condition of the machinery already in use Harvests of grains and sunflower seed were about half those of 1940, and that of sugar beets about one-third <sup>62</sup> Conditions were considerably better in 1947 and yet harvests ran only about three-quarters as great

<sup>62</sup> *Ibid.*, p. 60

as those of 1940 and left much to accomplish if goals for 1950 were to be reached<sup>63</sup>

The Soviet government in 1947 was doing everything it could to furnish farmers with incentives to put forth their maximum efforts. Medals and honors were provided for farmers who distinguished themselves in connection with acreages and yields. Socialist competitions between farms were arranged. A new official was created at each Machine Tractor Station—Vice-Director for the Political Section, whose duty is to see that the workers at the Machine Tractor Stations and the farms they serve do their work properly and according to plan. The remuneration system was altered so that collective farmers obtaining high yields will receive more income per labor day than others who are less successful. The pay of tractor and machine operators was made to vary according to the success with which planned yields are obtained on the farms they serve. Technical personnel working directly in the fields with the farmers were given a 25 per cent wage differential over technicians functioning in a purely administrative capacity.<sup>64</sup>

Finally, a new Council for Collective Farm Affairs was set up, headed by a member of the Politburo and including other high government officials and a few chairmen of collective farms. The Council is an enforcement agency for all legislation affecting collective farms and will see that punishment is meted out to violators. It hears complaints by members and officials of collective farms and takes action on them. It recommends legislation to improve the operation of collective farms. To facilitate the performance of its duties, the Council is allowed to have representatives in all major governmental subdivisions of the country.<sup>65</sup>

#### QUESTIONS

- 1 The organization and operation of agriculture in leading capitalistic countries is different in several respects from that of industry." Explain.
- 2 "The United States, in common with some other countries, has had an agricultural problem in recent years." What has been the nature of this problem?
- 3 "The government of the United States under capitalism has produced only palliatives and not a cure for the agricultural problem." Explain.

<sup>63</sup> *Ibid.*, p. 63.

<sup>64</sup> *Ibid.*, pp. 62-63.

<sup>65</sup> *Ibid.*, p. 57.

- 4 "To the leaders of the Soviet Russian regime, agriculture presented some of the most difficult of all the problems encountered in the attempt to socialize the means of production" Explain (1) why this statement is true and (2) how Soviet Russia handled the problems of agricultural organization
- 5 Describe the process by means of which much of Russian agriculture was collectivized during the period of the First Five-Year Plan
- 6 Compare the organization of state farms with that of collective farms in Soviet Russia. Would you expect the state farms or the collective farms to be more efficient? Why?
- 7 "The collective farms are merely being tolerated as a transitional form of agricultural organization in Soviet Russia. Eventually all of Russian agriculture will be converted into state farms" Show whether you agree
- 8 If you were to be an agricultural worker in Soviet Russia, would you prefer to be employed on a state farm or on a collective farm? Give reasons for your answer
- 9 Distinguish between compulsory and voluntary deliveries of the products of the Soviet Russian collective farms
- 10 What are the factors which determine how much income a member of a collective farm will obtain in return for his labor? Explain
- 11 In Soviet Russia the State Planning Commission makes plans for agriculture, as well as for other phases of economic activity, and yet most of the farms are run on a cooperative basis and not by the government itself. How is it possible for the government to control cooperative agricultural activities to such an extent that the State Planning Commission can make plans for agricultural production and expect that these plans will be carried out?
- 12 "The Russian planners control the operation of collective farms as completely as that of state farms, though by different methods" Show whether you agree
- 13 "At least two of the goals of the Russian planners for agriculture were achieved in large measure under the Five-Year Plans through 1940" Explain
- 14 "The results of planned operation in Soviet Russia were even more favorable for agriculture than for industry in the period from 1928 through 1940" Show whether you agree
- 15 Summarize the more important criticisms which were brought against the organization and operation of the collective farms in Soviet Russia prior to World War II
- 16 "The economic status of the agricultural population of Soviet Russia improved immensely under the Five-Year Plans through 1940" Do you agree? Explain
- 17 "Soviet Russian agricultural production was very well maintained during World War II" Show whether you agree
- 18 "Familiar types of abuses were apparently present in the operation of Soviet Russian collective farms during World War II" Explain

- 19 What steps has the Soviet Russian government taken in recent years in order to improve the operation of the collective farms and eliminate abuses therein? Explain
- 20 What are the goals of Soviet Russian agriculture under the Fourth Five Year Plan, and how much progress had been made toward these objectives through 1947?

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## CHAPTER 10

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### *AGRICULTURE*

*(Continued)*

#### *Agriculture in Britain under Partial Socialism*

*The General Plans for Agriculture* Agriculture is one of the many industries which remain under private ownership and management in Britain under partial socialism, but the affairs of the industry are under virtually complete governmental planning and control. The general plans are made by the Cabinet, including especially the Minister of Agriculture, and the Economic Planning Board. For the first five years of socialist rule, these plans aim at increasing net agricultural output by 400 million dollars, or 20 per cent, by 1951-52. The attainment of this goal will represent an expansion of output of 50 per cent by comparison with prewar output and of 15 per cent compared with the wartime peak of 1943-44. Half of the increase in output is expected to come from improvement in efficiency and the remainder from additions to the resources of the industry.<sup>1</sup>

The expansion in output is not to be at all uniform from one product to another, but rather will be concentrated in dollar-saving products, such as pork, beef, eggs, cereals, and linseed. This emphasis is different from that of the wartime agricultural program when the British were interested primarily in saving shipping space. Many thousands of additional workers will be required by the program and will be recruited from both British and foreign sources. Much new housing for the workers will be required and agriculture, along with coal mining, will have high priority in this respect. Allocations of materials are being revised so that agriculture will be able to get necessary machinery, equipment, supplies, and

<sup>1</sup>*Labor and Industry in Britain*, November December, 1947, pp. 224-225

construction materials The government is also furnishing technical advice to farmers

From the financial point of view, the government will furnish a large sum annually to finance the purchases of livestock, machinery, and other means of production It has permitted increases in the prices of farm products to enable the farmers to recover increases in costs due to agricultural wage increases and other factors and to provide a measure of confidence and stability for the farmers It has established a considerable variety of cash and other subsidies and acreage payments to encourage the farmers to do various things which are in line with the general plans

*The Regimentation of the Farmers* The detailed implementation, administration, and enforcement of the plans for agriculture are in the hands of the 10,000 members and officials of the County Agricultural Committees, which are appointed by and responsible to the Minister of Agriculture According to the official prospectus, these Committees are "to guide farmers in reaching their production targets, and to assist them by the provision of services and facilities"<sup>2</sup> Actually, the Committees seem to tell the farmers what to do and when to do it They can order the farmer to grow any type of crop even though he knows it will not pay They can order him to carry on cultivation by any kinds of methods even though he knows from experience that they are unsuited to his situation They can tell him to have certain operations carried out by certain dates and make the orders stick They can order the farmer to hire more workers and house them whether or not he needs them and can afford them In similar fashion they can order him to buy quantities of expensive machinery and equipment or to buy and apply large amounts of fertilizer<sup>3</sup>

Since 1939, all indigenous food supplies, with the exception of fish and green vegetables, have been purchased from the producers by the Ministry of Food or licensed buyers Prices to agricultural producers are set by the government, and supplies to farmers are allocated in such a way as to encourage sales from farms The government forbids farmers to feed millable grain to animals or to slaughter livestock without license It is officially admitted that there is something of a black market in agricultural products, but it is

<sup>2</sup> *Ibid.*, p. 226

<sup>3</sup> *The Chicago Tribune*, May 17, 1948

contended that its size is negligible in comparison with that which exists in some other European countries.<sup>4</sup>

Out of the operations and orders of the agricultural bureaucracy have come some of the usual comic results such as the order that metal disks be attached to the horns of pedigree Angus bulls being exported (though Angus bulls have no horns), and the regulation governing the picking and sale of green onions which regarded the

TABLE 9.

*INDEX NUMBERS OF CROP AND LIVESTOCK PRODUCTION IN BRITAIN  
IN SELECTED YEARS IN COMPARISON WITH PLANNED ESTIMATE  
1937-1938 = 100*

Item	1913-44 (actual)	1916-17 (actual)	1931-52 (planned)
Wheat	209	119	160
Barley	215	257	274
Oats	158	150	156
Potatoes	202	209	129
Sugar beets	137	164	131
Milk	101	107	123
Eggs	61	78	152
Beef and veal	83	93	110
Mutton and lamb	79	70	77
Pork	37	32	92

SOURCE: *Labor and Industry in Britain*, November-December, 1947, p. 22.<sup>5</sup>

farmers with the information that diameter shall be construed as meaning the maximum diameter of the bulb measured at right angles to the axis through the bulb and shoot. But much of the governmental control is not nearly so funny. The Committees and the Minister of Agriculture can invoke severe penalties against farmers for the disobedience of orders or other evidence of bad husbandry. Tenant farmers can be evicted and owner occupiers made to quit their land and lease it to other persons approved by the bureaucracy. Indeed, farm owners can be compelled to sell their farms to the government if the Minister of Agriculture certifies that he is satisfied that the farms are not being satisfactorily managed.<sup>6</sup> From the outbreak of the war to September, 1947, more than 11,500 farmers were accused of bad husbandry and thrown off their land.<sup>7</sup>

<sup>4</sup> *Labor and Industry in Britain*, March 1947, p. 55.

<sup>5</sup> *The Chicago Tribune*, September 5, 1947.

*Agricultural Production in 1946-47* The index numbers in Table 9 show the actual level of production of several important crops and types of livestock products in Britain in 1946-47 (June, 1946 through May, 1947), in comparison with the peak war year, 1943-44, and with planned estimates for 1951-52. A comparison is also afforded with 1937-38, since the level of output in that year is taken as 100 in all cases. In Table 10, we show the harvests of a

TABLE 10

*HARVESTS OF IMPORTANT CROPS IN BRITAIN AND QUANTITIES OF LIVESTOCK ON HAND IN SELECTED YEARS*

Item	Unit	1939	1943	1947
Wheat	Thousand tons	1,645	3,447	1,672
Barley	Thousand tons	892	1,645	1,621
Oats	Thousand tons	2,003	3,064	2,463
Potatoes	Thousand tons	5,218	9,822	7,766
Sugar beets	Thousand tons	3,529	3,760	2,886
Turnip and swedes	Thousand tons	10,076	11,991	9,221
Cattle	Thousand head on hand	8,872	9,616 <sup>a</sup>	9,559
Sheep	Thousand head on hand	26,887	20,150 <sup>a</sup>	16,748
Pigs	Thousand head on hand	4,394	2,152 <sup>a</sup>	1,629
Poultry	Thousand head on hand	74,357	62,136 <sup>a</sup>	69,954

<sup>a</sup> 1945 figure

SOURCE *Statistics on Britain's Position*, February, 1948, p. 5

number of important crops and quantities of livestock on hand in 1947 in comparison with 1939 and 1943. Examination of the available data indicates that prodigious increases in production will be necessary for some items, slight increases in others, and actual decreases in others, if the 1951-52 targets are to be attained. How well these adjustments will be made remains to be seen.

### *Agriculture under Fascism*

The fascist leaders of Germany and Italy professed to regard the farmers and their families as particularly worthy people and deserving of special treatment. The agricultural population had never succumbed to the lures of socialism, communism, and other radical movements as many of the industrial workers had. Indeed, the agricultural segment of the population in each country had been a mainstay of the fascist movement. The leaders also noted with

approval the fact that the birth rate among the agricultural population was well above that for other groups, and a large population seemed indispensable for a great and warlike nation. Finally, an expansion of agricultural production was essential to any fascist dreams of an economically independent and self-sufficient country. For all these reasons the fascist leaders designed to recognize the great significance of the "man on the land" to the development and progress of the nation, and they lost no time in instituting a program supposedly designed for agricultural improvement.

*Land Reclamation and Resettlement.* If the fascist leaders had really wanted to help the farmers of their countries, it would not have been difficult to find something useful to do. In both countries the chief obstacle to the welfare of the average farmer was undoubtedly the lack of an adequate amount of land. According to the 1930 census, 36 per cent of Italian farms had less than 25 acres of land and 91 per cent were under 25 acres in size. This 91 per cent of the farms had only one-third of all the farm land. Two-thirds of all the farm land belonged to 9 per cent of the farms and to 34 per cent of all landowners. Almost half the farm land belonged to one-half of one per cent of the agricultural population.<sup>6</sup> In Germany, landowners possessing estates of 5000 hectares or more made up only 0.15 per cent of the total number, but they owned altogether over 10 million hectares, or almost 40 per cent of the total land in cultivation. At the other end of the scale, 3 million small farmers and their families owned altogether only 1½ million hectares.<sup>7</sup>

Thus, with millions of small farmers needing more land badly and with large landed estates often poorly utilized and bursting at the seams with debt, it would have been logical to break up some of the large estates and distribute the land among the poor peasants. This was actually one of the proposals of the Italian Fascists in pre-revolutionary days, but it was soon dropped after the party came into power. In Germany, however, there was a great fanfare about returning the people to the land and finding them some land to which to return.

The Nazi leaders noted with horror that in the last half-century the composition of the German population had changed from 70 per cent rural and 30 per cent urban to 30 per cent rural and 70

<sup>6</sup> C. T. Schmidt, *The Corporate State in Action*, p. 113.

<sup>7</sup> *In Fact*, January 25, 1913, p. 2.

per cent urban.<sup>8</sup> This rather sudden urbanization of the German population created a very serious problem, according to the Nazi leaders. In the city, so it was said, the mind brightens, the critical faculties develop, and sciences flourish. Families get out of touch with the soil, lose their fundamental German ideas and outlook, become greedy, and pursue relentlessly money and wealth. The women invade offices and industries, and people forget their place in life and become sterile, so that births decline. Labor congregates in large numbers, learns the principles of organization and mass action, and becomes revolutionary. The Nazis held that the natural life of all true Germans is found in contact with the soil and that the only real solution for all internal unrest centering around what is called the "class struggle" was to be found in returning all labor to the land.

Specifically, this means giving every laborer some land, however small, and attaching him, through his new glebe, simultaneously to his "nature-chosen" occupation (agricultural or industrial) and to his locale. These adjustments are to be dovetailed with other programs whose net effect will be to regiment every workman according to his assumed capacities, and then so to "ordinate" his spirit that he will perform duly allotted "duties" with a minimum of friction and without desire to alter his status.<sup>9</sup>

In support of the agricultural section of the settlements program, the Nazi leaders argued that small farms are technically more efficient than large estates, that small peasants are more national-minded, more reliable in time of war, and more stable in periods of crisis, and that the development of the small peasantry would cause an expansion of the home market, would increase national self-sufficiency with respect to foods and raw materials, and would increase the population as the result of a high birth rate. Without pausing to evaluate these contentions, we may note that the real reasons for the rural program were probably (1) to counteract rural proletarianization and neutralize the threat of agricultural revolt, (2) to obtain a loyal peasantry as an offset to the radical urban proletariat, and (3) to promote the military defenses of the country through decentralization.<sup>10</sup>

<sup>8</sup> R. A. Brady, *The Spirit and Structure of German Fascism*, p. 269.

<sup>9</sup> From *The Spirit and Structure of German Fascism*, p. 281, copyright 1937 by Robert A. Brady, by permission of the Viking Press, Inc., New York.

<sup>10</sup> *Ibid.*, p. 278.

At any rate, the rural section of the program called for large estates to be liquidated and divided. The land was to be made into peasant farms of various sizes, under the Hereditary Farm Act, as well as into villages and community centers. The new farms were to be cultivated without hired labor. That is, all work was to be done by the farmers and their families, or through the various free labor services which the government furnished for the benefit of agriculture. The projects were to be financed with governmental credit, and the peasants thus created were to become a "geographically immobile, socially stationary, and property-minded petit-bourgeois class."<sup>11</sup> Actually, the rural settlements program did not amount to very much. Few estates were broken up and those were usually estates whose owners were bankrupt or wanted to sell out.

The other section of the settlements program was somewhat more successful. It involved two types of suburban settlements: (1) those placed more or less at random around the outskirts of large cities and (2) those clustered around large industrial plants and inhabited largely by company employees. Projects of the latter or "company-town" type existed even before National Socialism but were later extended. The Nazis made three types of persons eligible for the suburban settlements program: (1) workers whose incomes did not exceed the average of middle-class workers and tradesmen in the locality, (2) married workers, even though fully employed, with small incomes and at least four minor children, and (3) part-time workers employed less than 32 hours per week. The projects involved selling the workers plots of ground large enough for houses and gardens and building houses for them. Governmental assistance took the form of tax exemptions, low-cost loans, and outright grants or subsidies. In the case of the company towns, the loans to settlers were made secure by requiring the settlers to take out insurance policies in favor of the companies, and the companies could make payroll deductions for insurance premiums and regular payments on the loans. If the workers lived long enough and behaved themselves, they might eventually come to own their houses and lots.

The company town part of the program made rapid progress. By the end of 1937, industrial firms in the Rhine-Westphalia district controlled 240,000 houses and the Krupp company had constructed

<sup>11</sup> From *The Spirit and Structure of German Fascism*, p. 281, copyright 1937 by Robert A. Brady, by permission of The Viking Press, Inc., New York.

29,000 houses in connection with its Essen works alone, besides acquiring stock in three cooperative building associations and one building corporation.<sup>12</sup> Governmental investments in the other part of the suburban settlements program were not large. In about three years after the inauguration of the program in 1935, total expenditures amounted to only 446 million marks and the land affected amounted to only 0.03 per cent of the total cultivated area.<sup>13</sup> The settlements were supposed to be valuable in connection with the unemployment problem since reliable workers could be given part-time factory employment and be made to supplement their earnings with food products grown on their plots of land. The company settlements, besides furnishing a neat profit to the companies, were supposed to make the workers property-minded and bind them firmly to the enterprises for which they worked. In this way, labor turnover would be reduced, labor unrest would be neutralized by vegetable growing in spare time, wage cuts could be made with less worker resistance, and relief payments in times of depression would be reduced. In so far as the company settlements made for the decentralization of industry, an advantage would be gained in time of war.

The Nazi leaders also attempted to mend the "broken ties between men and the soil," and at the same time furnish almost free labor to agriculture, through the land-help system. The employment offices placed young men and women on the farms for limited periods of time, with food and shelter furnished by the farmers and a little pin money furnished by the employment offices. Men and women in the Labor Service were also required to spend a year on the land after completing their formal education. A series of decrees in 1934 and 1935 deprived unmarried men under 25 years of age of their jobs in the cities and required them to be sent to the farms as agricultural helpers, prohibited industrial enterprises and businesses from employing workers who had worked in agriculture during the preceding three years, and required such workers to be expelled from the cities and to be returned to the country or face criminal prosecution.<sup>14</sup>

In Italy, the emphasis was on land reclamation rather than on a settlements program. Land reclamation had as its aim the utiliza-

<sup>12</sup> *Monthly Labor Review*, January, 1939, pp. 99-102.

<sup>13</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 191.

<sup>14</sup> *Ibid.*, pp. 191-192.

tion of every available square mile of Italian soil by bringing under cultivation millions of acres of rocky sterile highlands and marshy wastes Although a land reclamation program had been under way long before 1922, it received a great impetus from the so-called Mussolini Act of 1928 which called for the expenditure of some 7 billion lire over a fourteen-year period Of this sum, 4 35 billion lire were to be furnished by the government and 2 65 billion lire by the landowners<sup>15</sup>

The reclamation program included projects for drainage, irrigation, reforestation, and road building, the provision of electricity and drinking water, and the construction of farm buildings Projects which were considered essential to the interests of the country as a whole were financed to the extent of 75 to 90 per cent by governmental funds, while other projects which were largely for the benefit of local landowners had only about 33 per cent of their expenses defrayed by the government The land to be reclaimed was divided into districts, and participation by landowners in each district was compulsory Each project was carried on by an association or consortium of landowners under governmental supervision and with the approval of the Minister of Agriculture and Forestry Land owners who were unable or unwilling to pay their share of the expenses of reclamation projects in their district could be deprived of their land

It is estimated that the Italian government invested about 8 billion lire in the reclamation projects from 1928 to 1935, after which the government had more pressing uses for its money About 5 million hectares, or almost one-sixth of the total area of the country, were affected by the projects, but substantial progress was made on only about 2 million hectares, including one project of about 500,000 hectares in the lower Po River Basin<sup>16</sup> The most spectacular project was the reclamation or drainage of the Pontine (or Pontine Marshes), a region of some 75,000 hectares of marsh and dunes within 60 kilometers of Rome Expenditures in this famous region were thought to have a greater publicity value than those in other parts of the country The draining of the Pontine Marshes was completed in October, 1940, according to the Italian government Some 50,000 hectares of wasteland had been brought into use

<sup>15</sup> C T Schmidt, *The Corporate State in Action*, p 106

<sup>16</sup> Eightieth Congress, First Session, House Document Number 401, *Fascism In Action* Washington Government Printing Office, 1917, p 139

and, in 1940, this land yielded 16½ thousand tons of wheat, 24 thousand tons of sugar beets, one thousand tons of cotton, and 5 thousand tons of sorghum.<sup>17</sup>

Opinions were divided as to the merits of the reclamation program in general and the draining of the Pontine Marshes in particular. Some writers regarded the draining of the Pontino, the building of new towns, and the settlement of people in the region, as almost miraculous. Critics pointed to the heavy cost of the reclamation program, which included many ill-advised projects. Much of the land in the Pontino and elsewhere was of very poor quality even after being reclaimed, and, by the end of 1935, only 2215 new units (19,048 individuals) had been settled in the Pontine region as against an announced goal of 40 to 50 thousand.<sup>18</sup> The reclamation program as a whole gave little relief to the land-hungry Italian peasants, for less than one-tenth of one per cent of all the land involved was taken away from the owners because of their refusal or inability to pay their share of the cost of reclamation, and the peasants were not given any preferential rights with respect to reclaimed land. However, the work provided by the program was of some assistance in connection with the problem of agricultural unemployment.

*The Category Corporations in Italy.* If the fascist leaders did not give their needy farmers more land, they certainly gave the farmers more governmental controls and regulations. In Italy, the controls were exercised largely through the category corporations. As we have seen, none of these corporations was organized directly in agriculture, but six of them represented branches of economic activity which involved agricultural, industrial, and commercial operations. These were the corporations of grains, horticulture, wines and edible oils, animal husbandry and fishing, wood and wood products, and textile products. The make-up of one of these corporations may be used to illustrate the composition of the others. Thus, the corporation of grains was made up of "A president and 36 members, including representatives of the Fascist Party (3), Grain Growers (7 employers', 7 workers'), Threshing Industry (1 employer', 1 workers'), Milling, Rice, Pasta, and Sweet-meat Industry (3 employers', 3 workers'), Breadmaking Industry (1 employer',

<sup>17</sup> Italian Library of Information *Business and Financial Report*, November, 1940.

<sup>18</sup> *Fascism in Action*, p. 140.

I workers'), Grain Trade (3 employers', 3 workers'), Consumers' Cooperative Societies (1), Agricultural Technicians (1), Artisans (1)"<sup>19</sup>

The early activities of these corporations were rather mild, as were those of the other groups of corporations. The corporation of grains discussed a standardized contract for the sale of flour, and tried to set up regulations for the distribution and sale of bread, for wheat markets, and for the flour industry. The corporation dealing with edible oils discussed the relations between the olive-oil and seed-oil industries, and the possibility of an official classification of olive oils. The corporation of horticulture discussed the standardization of vegetable products, the grading and packing of vegetables and their exhibition on export markets, new industrial uses of citrus fruits, and contracts between producers and dealers.<sup>20</sup> However, underneath all these seemingly innocuous activities lay a real possibility of governmental control over production, since the corporations could draw up rules and regulations governing all phases of productive activity, and these rules and regulations, after approval by the government, were binding on all producers with the force of law.

In later years, and especially after the beginning of World War II, agricultural production and marketing were severely controlled by the Italian government. In 1940, a decree was issued providing for the compulsory pooling for collective sale of all oats, whether imported or domestic, and authorizing the government to fix prices and conditions of purchase and sale. It was provided that 85 per cent of all wheat milled must go into bread flour. Wheat raisers were allowed to keep only 2 quintals (441 pounds) for consumption and the same quantity for seed. All the rest of the crop had to be delivered to the official pools. Farmers were given better prices (about 20 per cent higher) for wheat, corn, rice, and oats in 1940 than in 1939. At the official value of the lira, the new price of wheat worked out to \$2.34 per bushel. The selling prices for grains as quoted by the compulsory pools, remained unchanged, with the difference being made up by the government in order to increase farm income without raising the general cost of living. The old livestock markets were also abolished in 1940, and sellers were re-

<sup>19</sup> W. G. Weil, *Fascist Economic Policy*, p. 109. Reprinted by permission of the President and Fellows of Harvard College.

<sup>20</sup> *Ibid.*, pp. 120-121.

quired to bring their livestock to public markets where only three types of buyers were allowed—procurement agencies of the armed forces, the organization which provided meat dealers with stocks for direct civilian consumption, and the consortium which purchased meat for the meat-products industry. Sellers had to set aside 30 per cent of all cattle over 125 kilograms in weight for governmental use.<sup>21</sup> Such controls were continued and intensified in the later years of the war.

*The Agricultural (Food) Estate in Germany.* The general organization for the governmental control of agriculture under National Socialism was the Reich Agricultural Estate. This organization was set up in July, 1933, as a self-administrative statutory corporation. Membership was compulsory and included all individuals, associations, and agencies working directly in the field of agriculture, (or in forestry, hunting, fishing, market gardening, and viticulture), divided into five classes: (1) persons engaged in these lines of production or directly related to them, (2) agricultural unions, including their head organizations such as leagues of control, central unions, and other agencies, (3) all natural and legal persons who traded in the products of these fields of production or used them in manufacturing, (4) related organizations, such as the Council of German Agriculture, the Prussian Central Chamber of Agriculture, other Chambers of Agriculture, the National Bureau of Colonization, the Working Union of Rural Supply Companies, and the National League of Rural Sick Funds, and (5) marketing organizations and associations, including some eleven previously existing Central Associations for groups of products and many newly formed organizations for specific products. Thus, we see that dealers in agricultural products or other products which came under the Reich Agricultural Estate had to belong to this Estate as well as to that of Industry and Trade, while manufacturers using the same products had to belong to the Agricultural Estate as well as either to the Estate of Industry and Trade or to the Estate of Handicrafts. Membership in the Agricultural Estate could not be given up.

The head of the Agricultural Estate was the National Peasant (Farm) Leader, who was appointed by the Chancellor of the Reich (Hitler) and was responsible only to him. The National Peasant Leader in turn appointed lower officials of the Agricultural Estate.

<sup>21</sup> *Foreign Commerce Weekly*, November 2, 1940, p. 205, and December 7, 1940, p. 461.

and assigned duties and functions to them. He was, in fact, though not of necessity, the Reich Minister for Food and Agriculture as well. His term of office was indefinite and his control over the functioning of the Agricultural Estate was complete. The division of functions between the Reich Minister of Food and Agriculture and the same individual as National Peasant Leader was not clear, except that the Ministry performed various governmental administrative functions assigned to it by law, while the Agricultural Estate was thought of as "the coordinated self-expression of the members of the agricultural and commercial bodies and individuals closely concerned with agricultural products."<sup>22</sup> The Agricultural Estate functioned through three main divisions, 20 regional associations, 520 district associations, and numerous local associations.

*The Functions of the Agricultural Estate.* One of the main divisions of the Agricultural Estate dealt with "man," or personal questions relating to agriculture. It dealt with social relations in agriculture, legal matters, the attainment and maintenance of the proper attitude and point of view on the part of the farmers, and farm problems involving persons, the selection and settlement of new peasants, and land reclamation projects. The administration of the Hereditary Farm Act was carried on through this main division, but labor problems in agriculture were handled in other ways, since the Agricultural Estate belonged to the Labor Front. The second main division dealt with "the estate," or with questions of agricultural production. It controlled all functions and activities having to do with the farm as a productive enterprise. It controlled professional education, farm schools, agricultural science and experimental stations, the functions of agricultural chambers and societies, and the agricultural portion of the German economic self-sufficiency program.

The third main division of the Agricultural Estate had to do with "the market" and controlled the many marketing associations which had been set up for specific farm products. The marketing associations for specific products were organized along regional lines and the regional divisions were combined into central associations which supervised and controlled distributive activities all the way from actual production to sale to the final consumer, including financial and credit matters in connection with marketing. Operating under

-- M. Y. SIELEN, *The Structure of the Nazi Economy*, p. 181. Report of the Commission of the President and Fellows of Harvard College.

horizontal federations of enterprises who were at given stages of the productive processes, they saw to it that trading and marketing went on in accordance with rules of fair competition, standards of quality, and labels of quality identification. They had the power to license new enterprises or extensions of existing productive facilities. They had some control over production areas, conditions and terms of deliveries, costs of production, prices, advertising allowances, and profit margins of wholesalers, retailers, and manufacturers.

In addition to the marketing associations, government boards were set up which also had powers in connection with the control of prices received by farmers and processors of farm products and were responsible for the importation and exportation of farm products. The government boards were also trading agencies which bought and sold both domestic and imported farm produce. Anyone who wished to sell imported food in Germany had to obtain a permit from the appropriate government board and was required to turn over to the board the difference between the cost of the imported good and the higher price which prevailed in Germany. Domestic producers also needed permits to sell farm products and could be compelled to sell specified quantities of foodstuffs to the boards at fixed prices. In 1942, a new decree provided fines up to 100,000 marks, imprisonment, or even the death penalty, for farm producers who failed to turn over their marketable surpluses to the proper agencies of the government. Since they controlled the quantities and prices of imported farm goods, the domestic surpluses of such products, and the exportation of goods not needed at home, the government boards were able to exercise a strong influence on the domestic prices of these goods. To add to the confusion, however, it may be noted that the activities of the marketing associations and government boards in controlling the prices of farm products had to be brought into adjustment with those of the National Price Commissioner, who was in general charge of price control in Germany.

*The German Hereditary Farm Act.* The aims of the Nazis with respect to agriculture were by no means limited to controlling production, prices, and marketing, but included the creation of a peasant state of "Blood and Soil." Within this general aim, the farm program was designed to achieve three specific results—fixity of occupation, fixity of status, and fixity of residence. To achieve the

first of these results, a Hereditary Farm Act was passed which bound the "racially pure" Germans permanently to their land and their occupation. Fixity of status resulted from making the farmers into a definite and rigid social-economic class which occupied a position in the class structure of society which could be changed only at the will of the state. For German farmers who came under the Hereditary Farm Act, fixity of residence followed rather automatically from fixity of occupation and status. Other farmers were controlled by severe restrictions on immigration and emigration and on movements of persons between rural and urban areas.

According to the Hereditary Farm Act of 1933, farms which were large enough to be self-sustaining, that is, to support a peasant and his family, automatically became hereditary farms if they were owned by persons who could legally claim the status of peasant. To be a peasant within the meaning of the Act, the farmer had to be a German citizen, had to possess an "honorable character," and had to be able to show that his stock had been racially pure since January 1, 1800. The farmers' proof of racial purity had to be validated by court action. The size of the farms could vary from 20 to over 300 acres.<sup>23</sup> The farms were inalienable. They could not be divided up and distributed among several heirs, but had to be passed on intact, with all buildings and equipment, to the eldest son or the youngest son, according to local custom. The hereditary farms could not be sold to anyone and could not be mortgaged or otherwise encumbered by debt. They could not be taken by foreclosure under previously existing mortgages. The owners of the farms could obtain only short-term loans, based on their personal credit, and not in excess of sums which could be repaid out of current crop receipts. Thus, the owner could lose his farm only through governmental action, which might be taken if he were inefficient, became incapacitated, or failed to live up to the "peasant honor code." As previously noted, the Hereditary Farm Act was administered through the Reich Agricultural Estate Disputes concerning inheritance were decided by special Estate Courts, which were under the control of the National Peasant Leader. Some 650,000 to 700,000 farms were actually accepted as hereditary farms, as compared with a goal of 1,000,000.<sup>24</sup>

German agriculture, like other phases of economic activity under

<sup>23</sup> *Fascism in Action*, p. 187.

<sup>24</sup> *Fascism in Action*, p. 140.

fascism, appeared to be greatly over-organized. In the face of so many divisions, associations, and boards, it seemed difficult to get any clear picture of the actual functioning of the Agricultural Estate. In practice, its operation was simpler than it seemed for it was said that

The National Peasant Leader delegates or "entrusts duties" to his inferior designees, these delegate or "entrust" duties to other inferior officers. At the bottom of the scale the peasant is "delegated" or "entrusted" the duty of cultivating the land to the maximum advantage of "the people." In plain language, this means that the National Peasant Leader *tells* his designees what they are to do, these *tell* their inferior officers what to do, and these in turn *tell* the peasant, according to the law whether and what he may own, may produce, or may sell. Since the Nazi philosophy calls for complete "co-ordination of spirit and ideas," the same "delegating" or "entrusting" or commanding applies to social life, leisure time activities, and what the peasant, his family, and all rural labor may think, where they may go, and how they may feel about any thing which affects Germany, which is everything. Thus Nazi writers refer to as the 'new German freedom' <sup>25</sup>

*Agricultural Self-Sufficiency* One objective of both Italy and Germany under fascism was agricultural self-sufficiency. In Italy the campaign for self-sufficiency was typified by the "Battle of the Wheat," which was "to free the Italian people from the slavery of foreign bread." Italy, though an agricultural country, had long imported large amounts of wheat for domestic consumption. In the crop-year 1922-23, for example, Italian wheat production had amounted to 43.9 million quintals, while 31.4 million quintals were imported.<sup>26</sup> The Battle of the Wheat was intended to increase Italian wheat production so that the nation would no longer be dependent upon imports to any significant extent. The weapons of education and propaganda were poured into the battle, which began in earnest in 1925, and the government provided subsidies to stimulate the use of machinery and artificial fertilizers, and established low controlled prices for fertilizers and tractor fuel. The government also sponsored the building of silos, the use of selected seed, seed sorters, and motor ploughs, and the construction of drainage facilities, roads, stalls, and troughs. As these methods suggest, the battle had to be won largely by increasing production per hectare rather than by bringing large quantities of land under cultivation,

<sup>25</sup> From *The Spirit and Structure of German Fascism*, pp. 255-256, copyright 1937 by Robert A. Brady, by permission of the Viking Press, Inc., New York.

<sup>26</sup> W. G. Weik, *Fascist Economic Policy*, p. 195.

though some land was transferred from other uses to wheat-raising. However, devices such as heavy import duties on wheat, compulsory pooling of wheat outputs for sale, and flour-mixing regulations which required the use of a large percentage of home-grown wheat were even more potent weapons than those named above. These devices, of course, led to high wheat prices which were very stimulating to domestic production. The import duty on wheat itself was raised successively from 50 to 200 lire per quintal, or from 68 cents to \$2.70 per bushel and the flour-milling regulations required sometimes that flour should contain as high as 99 per cent of home-grown wheat.

According to the Fascist leaders, the Battle of the Wheat resulted in a glorious victory for Fascism. Wheat production per hectare of land, which had averaged 10.4 quintals from 1909 to 1914 and was only 9.5 quintals in 1922, increased to 15.4 quintals in 1935. Total wheat production, which in 1922 had stood at 88.2 on the basis of 1909-13 as 100, had reached 127.1 by 1935. Imports of wheat in 1934 were 2.6 per cent of the 1909-13 average, whereas in 1922 they had been as high as 238.1 per cent.<sup>27</sup> While these results seemed very encouraging, there were some other factors which led an outside observer to conclude that the Battle of the Wheat actually resulted in a Pyrrhic victory for Italy. In the first place, Italian agricultural conditions were greatly upset by the wheat campaign. The rotation of crops was neglected, and tree crops and livestock raising declined. Though the Italian climate and soil are well suited to the production of fruits, vegetables, nuts, and vines, the same soil cannot be used for these crops and for wheat as well. As wheat raising became more profitable than livestock raising, much pasture land was brought under the plow. Decreased imports of wheat, therefore, were offset to some extent by decreased exports of natural Italian fruit and vegetable products and by increased imports of such things as butter, wool, meat, and eggs. There is genuine doubt as to how much, if at all, the wheat campaign improved Italy's position with respect to self-sufficiency in foods and with respect to the balance of international trade.

The Battle of the Wheat proved to be of little benefit to Italian farmers in general. The gains were realized by the large landowners and already prosperous farmers, for only they had much wheat to sell at the artificially high prices which resulted from the wheat

<sup>27</sup> *Ibid.*, pp. 194-195.

campaign Small Italian farmers and tenants consumed ordinarily all the wheat which they raised and even had to buy additional quantities Thus, increased disparities between the large and small farmers and landowners were produced At the same time, the effects of the program were most serious for urban and rural workers and for consumers in general, since the high prices for wheat had a direct unfavorable influence on real wages and standards of living It has been estimated that the wheat campaign cost Italian consumers a net premium of 32 billion lire for the wheat which they consumed between 1925 and 1935 and that all this wheat, in the absence of the wheat campaign, could have been purchased for two-thirds of what it actually cost<sup>28</sup> To put the same thing in another way, total Italian wheat consumption, which had amounted to 76.6 million quintals in 1924 and 78.9 in 1929, was only 57.9 million quintals in 1935 The Italian population in 1935 was 122.9 on the basis of 1909-13 as 100, but total wheat consumption in 1935 was only 101.6 with 1909-13 as the base period<sup>29</sup> It is clear that the Battle of the Wheat was "won" by reducing consumption as well as by increasing production In a country such as Italy in which wheat is the mainstay of the people's diet, a victory of this type was bound to be costly After 1935, the Italians went on winning the battle, with stringent rationing as an additional weapon in years in which the crop failed to come up to expectations, since foreign sources of supply were no longer readily available to Italy In 1940 and 1941, for example, the wheat crop was about a million metric tons, or 12 per cent, below those of 1938 and 1939, but, because of her participation in World War II, Italy had to get along as best she could on the basis of domestic production

In Germany, the National Socialist plans for general economic self-sufficiency (to be discussed in detail in a later chapter) assigned a rather important part to agriculture, for Germany had normally been dependent on other countries for about 20 per cent of her food supply as well as important amounts of agricultural raw materials The plans for agricultural self-sufficiency simply involved, as in Italy, attempts to increase farm production For example, farmers were asked to double the quantity of land used for raising fibrous and oil-bearing plants and to double the number of sheep raised for wool However, serious obstacles stood in the way of

<sup>28</sup> C T Schmidt, *The Corporate State in Action*, p 104

<sup>29</sup> W G Weil, *Fascist Economic Policy*, p 195

increasing agricultural production When the Nazis came into power, about 63 per cent of all the land in Germany was cultivated or meadow land, 27 per cent was in forests, 6 per cent was used for site purposes, and 4 per cent was moor and waste land<sup>30</sup> While it would have been possible to reclaim some of the moor and waste land, the costs involved seemed likely to be prohibitive Clearing the forest land would have helped with ordinary farm production but would soon have impaired German self-sufficiency with respect to timber Increasing the number of sheep from 35 to 50 millions would have made Germany self-sufficient in wool production but would have required the withdrawal of much land from ordinary agricultural purposes to be used for pasture

In general, increased production in one sector of agricultural production seemed likely to involve decreasing production in some other sector About the only method for increasing agricultural production in general seemed to be the more intensive cultivation of the land already in use However, the German cultivated land had been inadequate from the beginning and it was already intensively cultivated Improved methods of cultivation, on the other hand, would have involved the use of expensive machinery and fertilizer, and it was difficult to see how the German farmers could obtain these things In spite of all obstacles, however, German agriculture made some progress toward self-sufficiency A small amount of waste land was reclaimed and brought into use, but simple hard work played the largest part in bringing about increased agricultural production

*Agricultural Output under Fascism* In Table 11, we show the production of some leading German agricultural products in the late 1930's in comparison with average production from 1932 to 1937 While the production of some of the products increased more than that of others, the general improvement in production is obvious On the whole, it has been estimated, if the physical volume of agricultural production in 1928 is taken as 100, that for 1932 was 106 and that for 1938 was 115<sup>31</sup> Again, the value of all agricultural production in 1939 was one billion marks (7 per cent) greater than in 1938 and 55 billion marks greater than in 1933<sup>32</sup>

<sup>30</sup> R. A. Brady, *The Spirit and Structure of German Fascism*, p. 267

<sup>31</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 206

<sup>32</sup> *Facts in Review*, June 3, 1940, p. 236

Governmental aid also played a part in the progress of German agriculture toward self-sufficiency. This aid took the form of large cash subsidies and other types of grants. Typical of the other grants was the governmental program for stimulating hog raising in 1940. Early in the year, the government entered into contracts with the farmers which called for the farmers to raise an additional 1½ million hogs to weigh at least 110 kilograms each and for the gov-

TABLE II

*PRODUCTION OF SOME LEADING GERMAN AGRICULTURAL PRODUCTS IN RECENT YEARS IN COMPARISON WITH 1932-37  
AVERAGE PRODUCTION*

Item	Unit	1932-37 Average	1938	1939	1940
1 All grains	Million tons	25.77	26.36	27.43	24.60
2 Wheat	Million tons	5.41	5.58	5.59	
3 Rye	Million tons	8.88	8.61	9.38	
4 Barley	Million tons	3.92	4.25	4.24	
5 Oats	Million tons	6.56	6.36	6.82	
6 Other grains	Million tons	1.00	1.56	1.40	
7 Potatoes	Million tons	46.8	50.9	51.5	60.0
8 Sugar beets	Million tons	10.9	15.5	15.6	20.0
9 Mangolds	Million tons	35.3	38.4	36.5	
10 Pigs on hand	Million head	22.3 <sup>a</sup>	23.6	24.8	
11 Sheep on hand	Million head	4.7 <sup>a</sup>	4.8	4.9	
12 Hens on hand	Million head	85.4 <sup>a</sup>	88.6	89.5	

<sup>a</sup> 1937 figure.

SOURCES: *The Economist*, December 9, 1939, p. 376; *Foreign Commerce Weekly*, November 9, 1940, p. 251.

ement to furnish 200 kilograms of barley or corn and 175 kilograms of sugar-beet flakes for each hog. In December, contracts were drawn up for an additional 900,000 hogs.<sup>33</sup> Again, progress toward self-sufficiency did not depend entirely on increased agricultural production, for natural and artificial substitutes were developed to replace agricultural products in whole or in part. Large quantities of "acorn meal" were used in making chocolate, low quality vegetable fats in making edible fat compounds, mineral oils in making soaps, and artificial textile fibers in making cloth.<sup>34</sup> The progress toward agricultural self-sufficiency had the usual re-

<sup>33</sup> *Foreign Commerce Weekly*, December 14, 1940 and January 4, 1941.

<sup>34</sup> R. A. Brady, *The Spirit and Structure of German Fascism*, p. 265.

sults in terms of high prices for goods, lowered qualities of goods, and decreased standards of living for consumers.

The statistics for the output of leading Italian agricultural products in selected years, as shown in Table 12, indicate the considerable expansion which occurred in the production of wheat, other grains, sugar beets, and potatoes. On the other hand, the production of citrus fruits, wine, and olive oil increased only slightly or declined somewhat over the years. If statistics for nuts, livestock, and other products were shown, they would also indicate stagnation or decline as a result of Fascist emphasis on wheat raising and the production of other common food crops.

TABLE 12

*PRODUCTION OF LEADING AGRICULTURAL COMMODITIES IN  
ITALY IN SELECTED YEARS, 1922-40*

Item	Unit	1922	1927	1932	1937	1940
1 Wheat	Million quintals	44.0	53.3	75.4	80.6	70.0
2 Rice	Million quintals	4.6	7.0	6.6	7.4	8.5
3 Corn	Million quintals	19.5	22.2	30.2	30.7	35.0
4 Sugar beets	Million quintals	22.6	20.2	24.9	33.1	
5 Potatoes	Million quintals	14.6	19.5	28.4	28.7	
6 Citrus fruits	Million quintals	6.8	6.6	11.6	6.8	
7 Wine	Million hectoliters	35.6	35.7	45.4	34.0	
8 Olive oil	Million hectoliters	2.8	1.6	2.3	3.0	

SOURCES W. G. Welk, *Fascist Economic Policy*, p. 196, *Foreign Commerce Weekly*, November 2, 1940, p. 205, and the *Economist*, March 15, 1941, p. 16.

*The Status of the Farmers under Fascism* A relatively small number of peasants may have had their hunger for more land satisfied, some farmers (especially in Germany) obtained a measure of debt relief at the cost of being bound hand and foot in their occupation and residence, and there were higher prices for farm products for those farmers who had produce to sell in Germany and Italy under fascism. On the whole, however, fascist agricultural policies did little to improve the lot of the small farmers and average farmers. Even the increases in prices of farm products did not suffice to give the farmers an increasing share of the national income. In Germany, agriculture and forestry received 8.3 per cent of a total national income of 46.6 billion marks in 1933, but in 1938 received only 7.3 per cent of a national income of 79.7 billion marks.<sup>55</sup> The

<sup>55</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 208.

total number of marks received by German agriculture and forestry thus increased sharply from 1933 to 1938, but their share of the national income declined. The fascist farmers paid a part of the cost of the armaments program and the construction of facilities for producing substitute goods.

On the other hand it must be said that, outside of being subject to increased regimentation and control, fascist agricultural policies did relatively little damage to the farmers and they suffered less than most groups in the population under the fascist regime. In Italy, of course, this result was practically automatic, for the status of the small and average farmers was so lowly in the first place that it would have taken cleverly designed policies to do them any great harm. An investigation in the 1930's established that there were 3,479,000 habitations in the Italian countryside. Of these, the investigating authorities classified 276,810 as "uninhabitable" and 739,580 as "almost uninhabitable." About a third of the rural population lived in these dwellings. Some 30,000 persons were reported as living in caves and 300,000 to 400,000 in hovels of earth and foliage.<sup>30</sup> The hourly wages of farm labor changed very little in Italy under fascism. Year by year they ranged from 10 to 15 lire per hour for common male laborers. This was, of course, an hourly wage rate of from roughly 5 to 7.5 cents. In the face of a constant upward trend in prices in the later years of fascism, the real wages and scales of living of Italian farm workers undoubtedly declined somewhat from their previous low level.

If any class or group of farmers can really be said to have gained under fascist agricultural policies, it was the relatively small group of large farmers in both countries. In the first place, the fascist leaders left these farmers relatively undisturbed in the possession of their large estates. Again, the Hereditary Farm Act in Germany was supposed to apply only to farms of 125 hectares or less, but it turned out in practice that large estates could be made into hereditary farms on special application, if the public interest seemed to require it. Many owners of large estates, severely harassed by creditors, sought and obtained the preferred status provided by the Act. In fact, in several sections of the country, peasants with small landholdings were deprived of their lands, which were then combined to form large scale hereditary farms.

<sup>30</sup> W. Ebenstein, *Fascist Italy*, New York: The American Book Company, 1939, p. 201.

Most of the governmental cash subsidies to agriculture were received by the large landowners and prosperous farmers, and the same thing was true of other subsidies for the stimulation of agricultural production under the self-sufficiency program. The policy of raising the prices of agricultural products was not applied uniformly to all farm commodities. Instead the government raised prices most for grains and other commodities that were produced for the most part on the large estates, which could make use of scientific, mechanized farming methods. Finally, much of the land-help, or virtually free agricultural labor service furnished by the government, went to the owners of large or medium-sized farms. On the other hand, the status of rural workers and small peasants under fascism is indicated by the severe restrictive measures which the government had to impose in order to keep these people on the land. Fascist agricultural policies, on the whole, can be considered successful only in the sense that they operated to produce a large part of the results which the fascist leaders wanted. However, the program of agricultural self-sufficiency was far from completely successful in both countries, and the people had to go on extremely short rations once they were dependent entirely on domestic production.

#### QUESTIONS

- 1 "The Labor Government has made ambitious general plans for British agriculture." Explain.
- 2 "Agriculture, though remaining under private ownership and operation, is thoroughly controlled by the government in Britain under partial socialism." Show whether you agree.
- 3 "Agricultural production was booming in Britain in 1946 and 1947 and the goals for 1951-1952 will be attained easily." Discuss.
- 4 Describe the aims, methods, and results of the fascist policy of land reclamation in Italy.
- 5 What were the objectives of the settlements program in Germany under fascism?
- 6 "The National Socialist settlements program was divided into two sections." Explain.
- 7 What was the leading problem of the average farmers in Germany and Italy when the fascist regimes came into power? Explain.
- 8 How was governmental control over agricultural production secured in Italy under fascism?
- 9 Describe the organization and functions of the Agricultural Estate in Germany under fascism.

- 10 What were the effects of the operation of the Hereditary Farm Act in Germany under fascism?
- 11 How did the fascists attempt to "free the Italian people from the slavery of foreign bread?" Explain
- 12 "Victory in the Battle of the Wheat was very costly for the Italian people" Show whether you agree
- 13 "The Battle of the Wheat was won by reducing consumption almost as much as by increasing production" Explain
- 14 "The average Italian farmer derived great gains from the Battle of the Wheat" Do you agree? Explain
- 15 Discuss the methods and results of the program of agricultural self-sufficiency in Germany under fascism
- 16 What happened to agricultural production in Italy and Germany under fascism?
- 17 "Fascist agricultural policies greatly improved the economic situation of most Italian farmers" Show whether you agree
- 18 "If any class or group of German farmers can really be said to have gained under the policies of fascism, it was the relatively small group of large farmers" Show whether you agree

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## CHAPTER 11

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### *THE MECHANISM OF EXCHANGE*

ONCE economic goods have been produced in the more limited sense of the term, some method or other must be found of getting them into the hands of the people who will finally consume them. This process is usually called exchange, or distribution, though the use of the latter term is inadvisable since it is also used in economics to refer to the division or apportionment of the national income among the owners of the various productive agents. The individuals who engage in the process of exchange are producers just as much as those who actually "make" the commodities in the first place, but it is customary to discuss their activities separately.

#### *Exchange Activities under Capitalism*

**Forms of Organization** The organization of exchange activities under capitalism is ordinarily left rather completely in the hands of private individuals and firms. Wholesalers, jobbers, retailers, and many other functional types of middlemen may handle commodities on their way from original producers to final consumers. On the other hand, manufacturers are free to try to eliminate one or more steps in the exchange process if they wish. They can attempt to sell directly to the final consumers or operate their own retail stores. The enterprises which operate in the process of exchange may be organized as single enterprises, partnerships, corporations, or co-operative associations. Wholesalers may specialize in a single class of products or may carry a number of different classes of products. Retail stores, in similar fashion, may be general stores or department stores which handle an almost endless variety of goods, or specialty stores which deal only in a particular class of merchandise such as meats, hardware, or clothing. Indeed, specialty stores often handle merely a part of a particular class of merchandise, such as

men's shoes or women's clothes Individual stores may operate as independent units or they may be grouped together in combinations or chains under common ownership and management Stores may sell directly to customers at a central place of business or they may do business through the mails

In all this organization of exchange activities, there is very little governmental interference under capitalism Governmental units seldom own and operate enterprises in the general field of exchange, and they do not often attempt to control the forms which private enterprises take Occasionally, however, a governmental unit will attempt to discourage or eliminate a particular type of enterprise, such as chain stores perhaps, by means of discriminatory taxation or other devices

*Prices and Price Control* In theory, the prices at which economic goods are exchanged under capitalism are determined by the operation of demand and supply forces in the market and not by governmental action While it describes the actual process of price determination only roughly and approximately, a large and elaborate theory of price determination has been built up in general economics This theory attempts to show how prices are determined under all the various market conditions which may prevail, and it concludes that the individual enterprise under all market conditions attempts to turn out such a volume of output as will make marginal revenue equal to marginal cost, for this action will result either in maximum profit or minimum loss The whole theory of price determination, however, seems to be stated in terms of the manufacturing, agricultural, or other "form-production" level, and not in terms of the wholesale or retail level Apparently it is assumed that prices at the form-production level, once they have been determined on the basis of competitive, monopolistic, or other conditions, will be faithfully reflected in the prices charged by wholesalers, retailers, and other middlemen for the same goods, and that the distributive or exchange branches of production are usually organized on a competitive basis

The government of a capitalistic economy seldom attempts to control directly either the prices of specific economic goods or the price level for goods in general, but many regulative activities of a capitalistic government may have at least an indirect effect on the prices at which particular economic goods sell In the United States, the Sherman Anti-Trust Act and other anti-trust laws, in so far as

they are effective in eliminating or preventing monopolies and trusts, may have an influence on the prices which consumers will pay for a considerable number of goods. We should note, however, that the monopolies and trusts against which the government proceeds are usually located at the form-production level rather than the exchange level. The Federal Trade Commission was organized in 1914 and was given wide powers to investigate and prevent unfair competition in American industry and business. Its activities have had an undoubted effect on prices, and some of the practices with which it has dealt have been at the exchange level. Such practices have included the selling of rebuilt articles as new, giving and offering to give premiums of unequal value with the particular premiums received to be determined by lot or chance, advertising articles for sale at "slashed prices" while in reality usual prices are charged, and making false claims of "no extra charge for credit."

The control of railroads, motor carriers, and water carriers by the federal government under various transportation acts includes the power to control or actually determine rates and fares charged to the public by these transportation agencies. State governments, operating through Public Service Commissions, control the rates charged by public utility companies in many cases, along with other phases of public utility operation. The control of public utility holding companies by the federal government under the Public Utilities Act of 1935 may have an effect on the rates paid by consumers for the services of public utility companies. The federal government operates plants for the production of electric power through the Tennessee Valley Authority and uses these plants as "yardsticks" to determine how cheaply electric power can be produced and transmitted and to discover whether existing rates are fair and reasonable. Public utility companies in the Tennessee Valley area have quite commonly discovered, since the government plants began to operate, that they could afford to sell electric power at rates well below those previously charged.

The codes of fair competition, which were drawn up for hundreds of industries under the National Industrial Recovery Act, had an influence on the prices of many goods. The anti-trust laws were suspended in so far as any activities of business men which were legal under the codes were concerned and many of the codes had provisions which prohibited the sale of goods at prices below cost of production or other provisions which made price control possible.

The federal government, operating through the Agricultural Adjustment Administration, does not directly determine the prices of agricultural products, but no one seriously doubts that the AAA acreage allotments, marketing quotas, and commodity loans, have had a strong influence on the prices of farm commodities.

The Robinson-Patman Amendment to the Clayton Act, passed in 1936, forbids sellers to charge different prices to different purchasers of commodities of like grade and quality—unless such price differences make only due allowance for differences in the cost of manufacture, sale, or delivery—whenever such discrimination would lessen competition substantially (1) between any buyer and the discriminating firm, (2) between the less-favored and the more-favored buyers, and (3) between the customers of those buyers. Formerly, manufacturers often marketed part of their products at regular prices and sold the remainder to mail-order houses, chain stores, or department stores at low prices for sale under a different name, or otherwise discriminated for or against these types of marketing agencies, as compared with ordinary wholesalers, jobbers, and retailers. The Miller-Tydings Act of 1937 amended the Sherman Anti-Trust Act of 1890 so as to legalise contracts for the maintenance of resale prices of branded articles wherever such contracts are approved by state laws, as they are practically in all states. Price-cutting on branded articles, and in particular their use as "loss-leaders" by chain and department stores, had long been a source of annoyance, both to the manufacturers of the goods, who had tried by extensive advertising to build up good will for their products at regular retail prices, and to competing independent merchants who naturally found their own trade injured by such price cutting. In the face of all these examples and others which might be given, it seems clear that, while many governmental influences on the prices of individual commodities are indirect rather than direct, the notion that the government of our modern capitalistic system leaves the prices of individual economic goods free to find their own respective levels under the operation of market forces is little more than a polite fiction today.

In ordinary times, the government of a capitalistic economy is not likely to attempt the *direct* control of the general level of prices. In the United States, the Board of Governors of the Federal Reserve System has had certain powers for controlling the expansion and contraction of bank credit by means of raising and lower-

ing rediscount rates, engaging in open-market operations, raising and lowering the reserve requirements which member banks must hold against demand and time deposits, and other methods. Since expansions and contractions in the general volume of bank credit are thought to be important in connection with upward and downward movements of the general price level, these powers were supposed to give the Board of Governors, and indirectly the government, a considerable measure of control over the general price level. In actual practice, however, attempts to control the general price level by these means have proved to be relatively ineffective.

In the emergency created by World War II, the federal government soon attempted to control the prices of particular goods by means of price ceilings and other devices. When the United States actually entered the war, Congress passed the Emergency Price Control Act in January, 1942, and this made possible the direct governmental control of prices in general. In April, 1942, the so-called General Maximum Price Regulation was announced. It provided that the prices of most commodities and a great many services be "frozen" as of March, 1942. Foods of most kinds, clothing, fuel, furniture, and furnishings, hardware and agricultural supplies, rents, and many other types of goods (both material and non-material) were included in the thousands of articles covered by price ceilings. Later, wages and salaries and the prices of most commodities which had been exempted originally from the operation of the General Maximum Price Regulation were brought under control, and our general system of price control became quite similar to those which had been adopted earlier in some of the controlled economies.

Opinions differ sharply as to the success of wartime price control in the United States. Some people point with pride to the fact that the index number of wholesale commodity prices advanced only 29 points from 1939 to 1945, and only 7 points from 1942 to 1945, when production, and hence the volume of purchasing power in the country, were making new high records. Others, although conceding that price control stabilized index numbers of prices, contended that it did no such thing for the actual cost of living, which increased tremendously in the face of supposedly stable prices. The government price indexes took no account of the high, black market prices which people had to pay if they were to secure any supplies of certain scarce goods which virtually disappeared from normal

marketing channels. Neither did the price indexes show the effects of other practices which business men devised for getting around price controls. Articles of some kinds could be obtained at ceiling prices only by buying them in combination with other goods whose prices were not controlled and were therefore exorbitant. Minor changes in articles converted them into new commodities whose prices were not subject to the original ceilings. Commodities were upgraded, articles of lowered quality were sold at the ceiling prices for goods of the old higher quality, and the quantities contained in packages of some goods were reduced while the prices remained the same. Manufacturers, given quantities of materials to use at their discretion, concentrated on the more profitable, higher-priced lines rather than the lower-priced types of commodities. Allowances for trade-ins were cut to the bone, and former discounts from established prices were forgotten. As a result of such developments it is possible to conclude that general price control, apart from the official price indexes, is not likely to work too well in an economic system in which businesses are privately owned and operated and business men are supposed to operate for profit.

*The Control of Consumption.* The government of a capitalistic economy does not, in general and in ordinary times, attempt to control the consumption of various economic goods by the individual citizens. Instead, the individual citizens, on the basis of their money incomes, are supposed to be able to choose freely from among the various commodities and services which are available on the market and cast their "ballots of the market place" for any goods which please them and are within their means. Since there is likely to be great inequality in the personal distribution of money income under capitalism, this means that some persons can command much greater quantities of economic goods than others. The resulting apportionment of goods is probably not of such a nature as will produce the greatest sum total of want satisfaction in consumption, and the government of a capitalistic economy may see fit to reduce inequality in the personal distribution of money income to some extent through income taxation, but, in general, the notion that the largest quantities of economic goods should go to the individuals who can command the greatest money incomes is not severely disapproved in a capitalistic system.

While the arbitrary allocation of quantities of consumers' goods to the individual citizens by means of rationing would be foreign

to the nature of a capitalistic system in normal times, a considerable amount of rationing may be necessary in periods of emergency. In the years after the entry of the United States into World War II, many commodities were brought under rationing by the federal government. Gasoline was rationed by making small allowances to all car operators for ordinary driving and then giving additional quantities to various types of persons for whom extensive transportation by automobile seemed to be in the public interest. In the case of tires, tubes, and new automobiles, no provision at all was made for ordinary civilian uses, and the entire available stocks were reserved for essential purposes. Sugar, coffee, and shoes were rationed among individuals by means of ration books which permitted the purchase of given quantities in given periods of time. Meats, fats, and oils, and canned, frozen, and dried fruits and vegetables were rationed on the basis of a complicated point system which involved the use of a second set of ration books.

Such rationing by physical quantities is certainly no more efficient than the usual system of rationing on the basis of price changes, but it is thought to furnish a more equitable means for sharing the limited supplies of various commodities in an emergency period. However, any notion that it substitutes complete equity among individuals for the inequity of operating on the basis of price changes should be abandoned with some haste. In our recent wartime experience, farmers who raised their own meat and were overburdened with fruits and vegetables available for canning were given just as many meat and canned goods coupons as the cliff-dwellers in city apartment houses who had to buy their entire supplies of these things. Individuals who could afford to eat out most of the time received as many food coupons as those who had to do all their eating at home. The same sugar coupons were given to those who baked at home and to those who purchased baked goods at stores and bakeries. Unless he could command the luxury of a "B card," the individual who lived three or four miles from his place of employment received the same gasoline ration as one who lived only a couple of blocks from his work. Individuals who did not like coffee and seldom required a new pair of shoes received the same number of coupons for these things as others whose tastes or needs were quite different. Real equity in rationing by physical quantities would require separate consideration of the situation of

each individual or family, but, of course, the ordinary emergency would be over before this could be accomplished.

### *Exchange Activities under Socialism and Communism*

*Exchange Activities under Socialism* The transition from capitalism to socialism, as the latter system is visualized in theory, would not alter exchange activities as much as most people might believe. To the extent that middlemen perform essential economic functions under capitalism, these functions would have to be performed by some agencies or other under socialism, whether or not the agencies were called by their capitalistic names. Since a socialistic economy would make use of money and prices, there would certainly be retail stores at which many kinds of economic goods would be sold to the consuming public. Private individuals might be allowed to operate small stores which involved no hired labor and wage slavery, and many other stores might be operated by cooperative associations, but most of the large and medium sized retail stores would probably be run by some governmental units or agencies. There seems to be no reason why a socialistic economy would not have general stores, department stores, specialty stores, chain stores, mail-order houses, and any other types of stores which exist in a capitalistic economy.

However, it is often contended that there would probably be fewer things passing through the marketing or exchange mechanism under socialism than under capitalism, because more things would be furnished directly and freely to the citizens by the government. The commodities and services supplied directly and without charge would include things which are communally supplied and consumed in any system (such as protection, law and order, factory inspection, and sewers), other intangible satisfactions which must be enjoyed by all citizens or by none (such as liberty, security, stability, equality), and perhaps many things which are sometimes if not always obtained by the individual citizens through sale and purchase in a capitalistic system (such as medical service, education, insurance, postal service, water, heat, light, aids to sight and hearing, milk, and possibly even meals).<sup>1</sup> In general, free and direct

<sup>1</sup> See for example, H. D. Dickinson, *Economics of Socialism*, pp. 51-59.

distribution might well be applied to any goods which are not likely to be used wastefully if free and which are likely to add to social welfare if they are consumed in increasing quantities. Such free, direct distribution would not be rationing, because each individual could obtain all he wanted or needed of the specified commodities and services. In the end, however, there would still remain a considerable range of commodities and services to be bought and sold in the exchange process.

Although many economic goods would have prices under socialism, both the prices of particular economic goods and the level of prices in general would have to be under close governmental control. It would be incompatible with the nature of a planned socialistic economy to permit the prices of individual goods to be determined by the unhampered action of market forces or to allow the prices of things in general to find their own level. To solve the general problem of price control, the economic planners would have to see to it that the total money income remaining in the hands of the citizens, allowing for taxes and other deductions, and available for spending was just enough to take the available quantities of commodities and services off the market at planned prices. At first glance, this would seem to be merely a problem in arithmetic, but in practice it would be quite complicated. The planners' calculations could be upset at least temporarily by the hoarding of money income or dissipating of hoarded money, and by the failure of production to meet planned schedules of output accurately after enough money income had been paid out to permit the purchase of planned quantities of goods. Moreover, it is one thing to give people enough money to buy given quantities of commodities but quite another thing to give them exactly enough money to buy the volume of services which a given quantity of productive facilities will turn out. Since a moving picture performance may play to 150 or 300 customers, a street car on a certain trip may carry 20 or 40 passengers, and a doctor may care for 10 or 20 sick people in a given period of time, it is difficult to know how much money income should be allowed to people for the purchase of services. Of course, this problem can be handled in part by removing the price tag completely from as many services as possible. The prices of individual goods under socialism would not play the important part which is theirs under capitalism in the making of general economic decisions, and it is only necessary that the planners set them at levels which are

compatible with the carrying out of the specific economic plans of the system for production and consumption. However, the result would be no perfectly stable prices for individual goods but rather a process of constant readjustment of these prices.

The rationing of consumers' goods has been a fairly common practice in the economic system of Soviet Russia, but there is nothing about the theoretical system of modern socialism which implies that this practice will be either necessary or desirable. Modern socialists agree that individuals in their system should be given money incomes which they can spend freely on any or all commodities and services which are available on a price basis, and that general rationing is undesirable. The question of how much freedom of consumption choice the consumer would have under modern socialism is a highly controversial one. In a capitalistic system, the individual consumer can get almost any good produced and furnished to him on the market if he is able and willing to pay enough for it. A socialistic economy, on the other hand, cannot undertake to furnish the individual with all commodities or services which he demands, because such a promise would be incompatible with the planned nature of the economy. The economic planners must decide, for better or worse, just what commodities and services are worth producing, and the consumption choices of the individual are limited necessarily to the range of commodities and services which the planners decree shall be placed on the market. Moreover, the individual is limited to a choice of consumers' goods and services in spending his income under socialism since, with very limited exceptions, he is not allowed to acquire productive wealth, such as land and capital.

On the other hand, it may be argued that, while the consumer under capitalism has a very wide potential or nominal range of consumption choices, most capitalistic consumers have such limited money incomes that their actual range of consumption choices is extremely limited. Mink coats and expensive limousines are available on the market under capitalism, but they are not within the range of choice of most individuals. Under socialism, the total range of consumption choices would be more limited and many things which are produced under capitalism might not be produced at all, but the money incomes of individuals would be relatively equal and each consumer would be able to buy virtually any commodity or service within the range of things which the planners saw fit to

put on the market Thus, it may be contended, the actual range of consumption choices would be greater for most individuals under socialism than under capitalism

***Exchange Activities under Communism*** The question of exchange activities under ideal communism can be disposed of briefly In this system, we are told, commodities and services would be produced and (in a sense) exchanged, but buying and selling activities would be completely eliminated The only exchange agencies that existed would be public storehouses to which individuals, who had produced according to their abilities, would come to help themselves without charge to commodities on the basis of their needs, and other places at which various services would also be dispensed without charge Prices and money, along with buying and selling, having been eliminated, there would be no question of controlled prices or any other prices Most descriptions of ideal communism seem to imply a very considerable degree of standardization or uniformity in consumption, with people living in the same kinds of houses, wearing standardized clothes, and consuming the same types of foods However, while the range of consumption choices might be limited under communism, in comparison with capitalism or even ideal socialism, the plan for the consumption of everything on the basis of needs and without charge is the very antithesis of rationing

### *Exchange Activities in Soviet Russia*

***Early Experiences*** All private trade in Russia was abolished by decrees of April 2 and November 21, 1918, and the distribution of commodities to the people was carried on through reorganized consumer cooperatives and governmental distribution centers With the introduction of the New Economic Policy in 1921, private trade and markets came into existence once more and flourished greatly In 1922-23, private trade accounted for 75.3 per cent of total retail business, as compared with 14.4 per cent for state trade and 10.8 per cent for cooperative trade About two-thirds of the private stores were one-man stalls or shops, and only about 4 per cent employed more than four sellers<sup>2</sup> On the whole, private enterprises in retailing were treated rather badly even under the New Economic

<sup>2</sup> A Baykov, *The Development of the Soviet Economic System*, p. 55

<sup>3</sup> L. E. Hubbard, *Soviet Trade and Distribution*, p. 14

Policy Private traders were barred from other occupations and from trade union membership, and then general position in a socialized economy was risky. Then business was hampered by discriminatory railroad rates and by governmental interference in deciding which districts should get industrial products and in what quantities. And all the while the government was encouraging the development of cooperative stores and laying the foundations for a large scale system of state stores.

*The Growth of State Marketing.* By 1928, private retailing establishments, while they still made up 77.8 per cent of the total number, handled only 22.1 per cent of the total volume of business. Governmental stores had only 15.9 per cent of the total trade, and cooperative stores did the lion's share of the business, 61.7 per cent.<sup>4</sup> In 1929, private trading was again abolished. By 1933, the governmental stores made up 28 per cent of the total number and controlled 44 per cent of the total retail business, the rest being handled by cooperative stores. In 1931, the right of the collective farms (and of individual peasants and collective farmers) to sell their surplus produce on the collective farm peasant markets was established. Competition between the cooperative stores and governmental stores continued until September 29, 1935, when a decree was issued excluding the cooperative stores from the 654 leading cities and towns, though they continued to function in rural areas. In 1938, there were 354,700 retail stores, as compared with over a million in 1912. The governmental stores handled 59 per cent of the retail trade in 1939, the cooperative stores 25.4 per cent, and the farm markets 15.6 per cent.<sup>5</sup>

*Cooperative Stores.* The cooperative stores continue to be of great importance in rural retailing, handling about 75 per cent of that business, with local cooperative associations running from one to five or more stores. The stores are both general and specialized. Some of the large stores have their own dairies, bakeries, and manufacturing plants to supply them with goods. Large cooperative stores (with a monthly turnover of 20,000 rubles or more) are financially autonomous, which means that they have their own accounts with the state bank and deal directly with the commercial departments of industries and other selling organizations in securing goods for

<sup>4</sup> A. Baykov, *op. cit.*, p. 65.

<sup>5</sup> L. S. Hubbard *op. cit.*, p. 37.

<sup>6</sup> A. Baykov, *op. cit.*, p. 254.

sale to their members Small cooperative stores are financed and supplied with goods by District Unions of Cooperatives These District Unions also operate their own stores, which sell a better variety and quality of goods than the small cooperative stores

**Governmental Stores** The stores which are run by various governmental units are almost all chain stores, but they fall into several general types In the first place, many governmental stores are run by *Toig*, which are autonomous governmental organizations of republics or provinces Some of the stores under a *Toig* may be small enterprises which are completely controlled by the *Toig*, while others are large stores with independent budgets, direct accounts at the state bank, and an extensive choice of goods Most of the stores operated by *Toig* are specialty stores In the second place, there are some All-Union *Toig*, which sell furs, jewelry, sporting goods, textiles and clothing, stationery, and other articles to high class consumers in the larger cities Thirdly, there are "universal magazines" or department stores which operate quite independently though they are under the control of various governmental units Fourthly, the federal government operates a series of All-Union Provision Shops These differ from the stores operated by *Toig* in that they handle the products of national food industries (such as manufactured cereals, patent foods, and canned and preserved foods) while the stores under *Toig* deal more in local fresh produce and the products of local food industries Both types of stores sell ordinary staple foods, however Finally, there are stores operated by the commercial departments of industries which are under the Ministries producing foods and manufactured consumers' goods These are often model or experimental stores, which seek to introduce new products and to measure the demand for various articles Besides the cooperative stores, governmental stores, and collective farm peasant markets, private individuals and producers' cooperatives in handicraft production are allowed to sell their own products, but private individuals are not allowed to operate trading enterprises which buy and sell goods

**Centralized Control of Marketing** In 1930, the marketing of goods in internal trade was transferred from the Commissariat of Trade to the Commissariat of Supplies The latter organization was divided into the Commissariat of Internal Trade and the Commissariat of Food Industries in 1934 The Commissariat (later Ministry) of Internal Trade was reorganized in 1936 so that it contained four

administrations, two for retail trading in different geographical areas, one for restaurants, cafes, and public dining rooms, and one for railroad buffets, dining cars, and ship canteens and restaurants. The functions of the administrations in internal trade are similar to those of the administrations in industry. Below the administrations are departments, which deal with the organization of trading enterprises, planning the distribution of industrial finished commodities, planning the distribution of foods, planning the turnover, personnel, conditions of employment, and capital construction of trading units, finance, trade inspection, training and educating personnel, statistics, special political duties, transportation, and economic administration. Also subsidiary to the administrations are three all-union governmental offices for wholesale trade in various goods, five all-union governmental offices for retail trading in various goods, and eight special all-union bureaus. There are also similar organizational hierarchies in the republics, provinces, regions, and cities.

The general principle which the planners have had in mind in connection with the distribution of finished goods has been to satisfy the consumption desires of various segments of the population in proportion to their significance to the economy as a whole. Assuming that production in general is fairly well suited to the needs and desires of consumers, the chief problems in the distribution of goods, apart from the general one of inducing efficiency in the operation of the various marketing enterprises, have been those of dividing goods among geographical regions so that effective demand in each area is satisfied to something like the same extent, distributing goods so that industrial workers and peasants are fairly well satisfied and continue functioning and furnishing goods to different segments of the population in reasonable accordance with racial and national habits and tastes. In trying to solve these problems, the planners must divide the total goods available into market and non-market funds. Goods in the non-market fund go into industrial consumption, further processing or manufacture, exportation, or consumption by the armed forces. The market fund at the end of the Second Five-Year Plan amounted to about 74 per cent of the total output of consumable goods.

The market fund is divided into planned and regulated sections on the basis of importance and adequacy of supply. The distinction between planned and regulated goods is found in the extent to

which their distribution is planned centrally. The planned goods include the more important consumption goods and the scarcer commodities, and their distribution is planned by the central authorities all the way down to their allocation to local trading organizations. The regulated goods are less scarce or less important, and they are merely allocated to the republics and central trade organizations, leaving the details of their distribution to be determined at lower levels. The market fund, of course, is divided among the various territorial units of the country, and the territorial allotments are divided between the urban and rural distributive systems. Finally, the goods are placed in the hands of actual retailing organizations and enterprises.

Such matters as the supplying of goods to individual stores and the selection or assortment of goods which individual stores should carry are difficult to plan at national headquarters. As a result, many stores are given a certain amount of freedom in ordering their goods on a contract basis. How much freedom an individual store is allowed to have depends on such factors as the size of its turnover, its importance, and the class of customers which it serves. Stores are required to post official price lists for their goods, however, and there are inspectors to see that they abide by official price and quality standards. On the other hand, the plans set no maximum limits on the amount of business which the stores may do and they are encouraged to expand retail trade to the greatest possible volume. Just how well the Russian marketing system has worked in practice will be seen after we have discussed price control and rationing.

*Price Control in Retail Markets* It goes without saying that prices are controlled in the Russian planned economy. All the really important economic decisions are made by means of economic planning and not on the basis of prices. Under these conditions, price control is a component part of economic planning in general and not something imposed upon an economy which would normally be expected to operate in some other fashion. Subject to the general directives of the Communist Party, the power of price control lies in the Council of People's Commissars and the State Planning Commission, though the detailed work of price fixing is done at various levels all the way from the Ministry of Trade through republican, district and local governmental units to individual trading organizations. Retail prices as finally set up, include wholesale prices,

turnover taxes, expenses (and planned profits) of the retail trade operations, and transport expenses.

Retail prices in general are intended to control the effective demand for consumers' goods so that consumption will keep pace with production. On this basis, the price of any given consumers' good should be maintained at such a level that the collective estimate of the good's desirability will coincide with the available supply. In this connection, it should be remembered that prices which are above or below the cost of production level do not necessarily stimulate or retard production. The planners reserve the ultimate right to decide what should be produced for the people, and their decisions do not necessarily agree with the collective opinions of the people. If the consumers show an increasing demand for some good whose production the planners would rather not expand, effective demand is limited by raising the price of the good.

Under the influence of extreme scarcity, the distribution of consumer's goods under the First Five-Year Plan and part of the Second Plan was largely on the basis of rationing. Several classes of stores were set up for selling rationed goods to different classes of purchasers, and the prices which prevailed in these stores were kept very low in comparison with the prices which would have prevailed in a free market. However, it was not always easy to adjust rations to compensate for changes which occurred in the production of consumers' goods, and on the whole there were not enough goods available to use up the entire money incomes of the people at the low fixed prices for rationed goods. The output of consumers' goods in terms of physical units increased only slightly, if at all, under the First Five-Year Plan but the wages and salaries of workers for governmental and cooperative enterprises more than quadrupled. The workers often found that there was nothing on which to spend the remainder of their money incomes after the rationed goods were purchased. This situation led some wag to remark that the Russian workers were the richest in the world since they had more money than they knew what to do with.

At any rate, the "commercial" stores which began to develop under the First Five-Year Plan furnished something of an outlet for the surplus money incomes of the workers since they would sell any quantities of goods to any purchasers, though at very high prices. The commercial stores handled only 3 per cent of all retail trade in

1932, but 15 per cent in 1933 and 25 per cent in 1934.<sup>7</sup> The differences in the prices of the same goods from the ration stores to the commercial stores were extremely large. In Leningrad and Moscow in 1931, the ration price of bread in workers' ration stores was one ruble per kilogram, but it was two rubles in the commercial stores. Sugar was four times as high in commercial stores as in workers' ration stores, tea three times, fish four times, soap two to five times, meat five to eight times, butter five to six times, and eggs five times.<sup>8</sup> This relationship between prices in the ration and commercial stores tended to make differences in real income among workers smaller than differences in their money incomes. If a worker who received 1000 rubles a year could spend all his income for rationed goods while one who received 5000 rubles a year could spend only 1000 rubles for rationed goods and had to spend the remainder in the commercial stores, the difference in real income between the two workers would be nearly two to one than five to one.

With the abandonment of rationing in 1935, both governmental and cooperative retail stores began to operate on a commercial basis. That is, they would sell any quantity of any available good to any purchaser at prices which were originally in between those which had prevailed formerly in ration and commercial stores. This change to the commercial basis in retailing was the result of many factors as we shall see. Under the new system, consumers' goods were supposed to sell at single government-controlled retail prices, but this did not mean that the prices of the same goods were uniform all over the country. Instead, they were uniform only within zones. Eight zones were established for bread and cereal foods, five for meat and fish, four for sugar and confectionery, four for vegetable oils, and five for butter. Differences in prices for the same goods may be as great as 25 to 100 per cent from the high to the low zones.<sup>9</sup> The differences are based in part on transportation and distribution costs and partly on other considerations such as regional self-sufficiency or the desire to encourage particular lines of production in areas.

There is really no pricing problem from the point of view of the individual retail enterprise. Both wholesale and retail prices are fixed from above and the difference is the gross profit of the retail

<sup>7</sup> L. E. Hubbard, *Soviet Trade and Distribution*, pp. 55-58.

<sup>8</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 206.

<sup>9</sup> L. E. Hubbard, *Soviet Trade and Distribution*, p. 195.

enterprise. From this gross margin, overhead and operating costs of the stores must be paid. The gross margin is supposed to be so contrived that the retail store which operates with normal but not exceptional efficiency will be able to make a small amount of net profit. Sometimes the gross margin has been permitted to be somewhat more favorable for some goods than for others, and the managers of stores, with some freedom to determine the assortment of goods which they will carry, have not unnaturally emphasized the goods which afford the larger margins of gross profit.

Though prices in general as well as those of individual goods are under governmental control in Soviet Russia, the general price level moved upward significantly during the years of planned operation from 1928 to 1940. The total money in circulation in 1928 was two billion rubles, and it was supposed to increase by not over 250 millions per year under the First Five-Year Plan, or to 3.25 billion rubles by 1932. The money actually in circulation by the end of 1932 amounted to 8.4 billion rubles. In 1932 alone, the money in circulation increased 37.7 per cent, while the national income in terms of goods increased by only 11.2 per cent. The money in circulation increased further to 11.3 billion rubles by the end of 1936, after which the publication of statistics on this subject was discontinued.<sup>10</sup> Prices did not skyrocket in this situation, because of governmental control, but there was undoubtedly inflation in the sense of a great increase in the medium of exchange not accompanied by a corresponding increase in the volume of commodities and services available for purchase and consumption.

It is difficult to measure the extent to which retail prices rose in this period of currency expansion. However, one writer has estimated the cost of the "Moscow weekly food basket" (as given in the family budget submitted to the Bureau of Labor of the League of Nations by representatives of Russian trade unions) for the beginning and end of this period. The basket cost 2.50 rubles in 1928 before the introduction of rationing, but in 1935 it cost 13.38 rubles in the ration stores and 34.82 rubles in the commercial stores. The monthly wage of the average industrial worker would have bought 29 such baskets in 1928, but only 13.9 baskets at the ration stores and 5.3 at the commercial stores in 1935.<sup>11</sup> After all the retail stores went on the commercial basis, the prices of some foods remained

<sup>10</sup> A. Yugov, *Russia's Economic Front for War and Peace*, p. 144.

<sup>11</sup> *Ibid.*, p. 207.

quite stable from 1935 to 1939 while those of others increased moderately. The market basket cost 19.20 rubles under the uniform price system at the end of 1935, 20.80 rubles in July, 1937, and 24.25 rubles in July, 1939. The average industrial worker, with one month's wages, could buy 9.6 baskets in 1935, 13.6 baskets in 1937, and 15.7 baskets in 1939.<sup>12</sup> However, prices rose rapidly in 1940, and by the end of the year the prices of many foodstuffs were two to four times as high as they had been in 1935. The prices of many manufactured consumers' goods rose considerably from 1936 to 1939. Men's suits went up 45 per cent, women's shoes 50 per cent, and woolen cloth 100 per cent.

The inflation of prices which occurred in the Russian planned economy is usually attributed to the fact that Russia made large increases in industrial production while experiencing construction costs that were much higher than had been expected and while failing to attain expected increases in labor productivity and decreases in costs of production. In this situation, the planners may have thought that the easiest way out was to permit the prices of consumers' goods to rise. On the other hand, it is sometimes alleged that the Russian planners attempted to use high and rising prices as the means of stimulating the maximum possible accumulation of capital. The increases in prices after 1939 were undoubtedly connected with the preparation for and participation in war. Whatever the causes may have been, it may be true that the significance of price inflation is not the same in Russia as in capitalistic countries because the government is in control of the distributive system, because rationing can be used, when necessary, to make sure that the ordinary citizens will be able at least to secure the necessities of life, and because there are no private debtor-creditor relations to be upset by changes in the price level.

*Rationing in Soviet Russia* The First Five-Year Plan provided for a high rate of capital investment and a great increase in the number of industrial workers. The total money income distributed to the population increased sharply, but the quantity of goods available for consumption could not be increased to the same extent because of the heavy capital investments, the exportation of commodities to acquire foreign exchange with which to buy machinery and hire technical experts and the many difficulties encountered in trying to carry out the plan. In the face of the shortage of consumable goods,

<sup>12</sup> *Ibid.*, p. 209

rationing was introduced to prevent an extreme inflation of prices and to provide the industrial workers in the cities with as high a standard of living as possible Rationing began in Leningrad in November, 1928, and in the next year was extended over the whole country By 1934, about 70 million persons were receiving rations<sup>13</sup>

In the beginning, rations were not thoroughly standardized and all members of consumer cooperatives had ration cards Four geographical classifications of rations were set up by 1930, with consumers in the largest cities getting the largest rations The holders of ration cards were divided into several classes in 1931 and separate ration stores were established to serve each group Thus, there were stores for Commissars, chairmen of the large trusts, leading Party officials, and members of central committees of the government, for members of the O G P U or secret police, for favored industrial officials, scientists, and engineers, for Red Army officers, for workers in factories producing capital goods, and for other types of workers These different ration stores made it possible to favor some groups at the expense of others, by varying the prices or the kinds, quantities, and qualities of goods available at the different types of stores Workers in heavy industry were favored in comparison with other workers, but the most favored group was composed of leading Party members and officials It is sometimes alleged that this latter group was always kept supplied with meat, milk, butter, eggs, fresh fruits and vegetables, cocoa, and chocolate, while many persons received only bread, flour or grain, and a little sugar In this situation, the "vow of poverty" on the part of Party members and the restriction of their money incomes to the level received by first-class industrial workers were said to be meaningless in practice Ranking Party members had also the use of cars, access to the best housing, and special hospitals and medical attention Having acquired a good apartment or flat for a reasonable rental, they were often able to sublet rooms for more than the rental cost of the whole establishment<sup>14</sup>

The rationed articles included bread, macaroni, grits, sugar, tea, sunflower-seed oil, oleomargarine, herring, fresh fish, flour, meat, butter, milk, soap, textiles, clothing, and many other commodities Some of these articles, as we have suggested, were distributed only to the higher ration categories In December, 1932, the issue of

<sup>13</sup> L E Hubbard *Soviet Trade and Distribution*, p 83

<sup>14</sup> F Utley, *The Dream We Lost*, pp 69 70, and 223 224

ration books to workers was turned over to the factories in order to attach the workers more firmly to their jobs and cut down labor turnover. By the end of 1932, about 50 per cent of all manufactured consumers' goods and a much higher percentage of foodstuffs were subject to rationing.<sup>15</sup>

Under the circumstances which existed at the time, the rationing of foods and other consumers' goods was probably desirable, though it produced some unfortunate results. The possession of ration cards did not insure the receipt of the rationed commodities unless the consumers could find stores in which the commodities were available, and this was often difficult to do. The Russian consumers, on the basis of sad experience, distrusted the distributive agencies, and the report that a good had become available at particular stores was often enough to start a grand rush to purchase it. Even the adding of a product to the rationed list would usually intensify the demand for it both on the part of those who really needed it and all others who were entitled to buy it. As a result, the Russian consumers spent a great deal of time standing in line at the stores to obtain their goods. Even relatively poor families, if both adult members were working, often had to employ domestic servants in order to have someone to do their standing in line for them.

It may be noted in passing, however, that goods often appear scarcer under a system of rationing by quantities than under a system in which the apportionment of goods among consumers occurs on the basis of price changes. When the price of a commodity is maintained at a moderate level in spite of the scarcity of the product, the appearance of a quantity of it in the stores may lead buyers to stand in long lines waiting for hours in order to buy the small quantities which they are allotted. On the other hand, when consumers' goods are apportioned on the basis of price changes, the fact that the stock of a good is limited will not make people stand in line to buy it if its price rises sufficiently. Consumers with inadequate purchasing power will realize that they cannot afford to buy the good in question and will see that there is no point in standing in line outside the stores in which the good is available for those who can afford it. Thus, the capitalistic method of apportioning goods among the citizens makes it appear that any amount of a good is adequate to care for the desires of the people who wish to

<sup>15</sup> L. E. Hubbard, *Soviet Trade and Distribution*, p. 35.

purchase it, even though in reality many people who want the good are excluded altogether from its consumption

The rationing system in Russia led also to very inefficient retailing. The stores were dirty and unkempt. Store employees were altogether too few in number and seemed completely indifferent to the wishes of the customers. The buyers were required to pay for their purchases before selecting them, commodities which required wrapping were left unwrapped, people had to bring their own cans or other receptacles in order to buy commodities which required these things, and, of course, there was no delivery service. There were too few stores and too little room in each one, goods were not marked with price tags, commodities were poorly displayed, and conditions of storage were frightful.<sup>16</sup> It often appeared that the goods were just thrown into the stores and many scarce consumers' goods spoiled before anyone was able to purchase them. All these conditions were possible because store employees and officials had little personal interest in the business and because, under the system of rationing, they were sure of their customers' business no matter how inefficiently the stores were operated. It was difficult to improve standards of efficiency in retailing so long as the system of rationing remained in operation.

The rationing of bread and flour ended on January 1, 1935, and the rest of the rationing system was eliminated by January 1, 1936. After this date, as we have noted, all the stores operated on the "commercial" basis. The rationing system was liquidated for several reasons. Foods and consumers' goods of other kinds were being produced in relatively more adequate quantities by 1935 and it was less necessary than formerly to use rationing to insure ordinary people the bare necessities of life. Opposition to the socialistic regime had died out to the extent that it seemed no longer necessary to use rationing to favor certain classes of people. With rationing ended, differences in money wages would represent differences in real wages more accurately than formerly, and this seemed desirable in the light of the Soviet principle of payment according to work done. It was easier to distribute workers among industries on the basis of differences in money wages than by manipulating rations. Finally, an increase in the efficiency of retailing was greatly desired. With all stores selling the same goods at the same prices in any quantities desired or available, the managers and employees of retailing estab-

<sup>16</sup> *Ibid.*, p. 242

lishments had to attend to business and do their best to attract patronage in competition with other stores, for their efficiency could now be estimated at least in part on the basis of their volume of business and profits.

*Evaluation of Russian Marketing through 1940* In support of the Russian marketing system, it must be said that the total volume of retail trade increased by leaps and bounds from 1928 through 1940. Disregarding sales on the farm markets, it increased from 15.2 billion rubles in 1928 to 35.5 billion rubles in 1932, 125.9 billion rubles in 1937, and 174.5 billion rubles in 1940.<sup>17</sup> These figures, of course, are in current rubles and do not show accurately the increase in the physical volume of trade, since prices rose considerably over the period. At any rate, the statistics seem to show too much, and one might wonder how the total retail trade for 1940 could have amounted to 174.5 billion rubles, for state and cooperative stores, when the total value of all consumers' goods produced in the same year was only 54 billion rubles. The answer is in part that the value of all consumers' goods is given as of the completion of their manufacture or processing, while large turnover taxes at varying rates and other costs are included in the prices of goods sold at retail.

In the second place, there can be no question that the efficiency of Russian retailing improved over the period in question. This, in a way, was an automatic accomplishment, because, if the quality of Russian retailing changed, it had to change for the better. Nevertheless, it is a far cry from the miserable stores of ration days to some of the modern retail establishments in the large cities, which have large varieties of goods, numerous and attentive sales people, tea rooms, restaurants, and nurseries. The stores are well decorated, display their goods in modern fashion, engage in some advertising, and wrap and deliver purchases.<sup>18</sup> Soviet authorities claim that the Russian stores operate with great efficiency since their costs for overhead and distribution are said to be no more than 11 or 12 per cent of sales, while a figure of 25 or 30 per cent is not uncommon in the retail establishments of capitalistic countries.<sup>19</sup> The Russian estimate is somewhat misleading, however, because costs are usually figured on the gross volume of trade which includes the turnover

<sup>17</sup> A. Brykov, *The Development of the Soviet Economic System*, pp. 235, 260.

<sup>18</sup> L. E. Hubbard, *Soviet Trade and Distribution*, pp. 211-242.

<sup>19</sup> *Ibid.*, pp. 202-203.

taxes, and costs are not really comparable as between Russian stores and those of capitalistic countries. The Russian stores pay low interest on funds borrowed from the government and little if any rent. They carry smaller selections of goods, give no credit to customers, limit advertising expense to a fraction of one per cent of gross sales, and often do not even provide delivery service.<sup>19</sup>

The Russian stores have some advantages in comparison with stores in capitalistic countries, because some of the higher costs of the latter stores are unnecessary and wasteful. The Russian stores can avoid the great and wasteful duplication of productive facilities in retailing which is so common under capitalism. Because the varieties of goods produced in industry are relatively limited, the Russian stores can avoid the unnecessary proliferation of styles, shapes, sizes, and colors of goods in which capitalistic stores indulge. Finally, the Russian stores limit their advertising to educational and informative varieties and do not waste large quantities of money and productive agents on advertising which is merely competitive or combative. Thus, the difference in costs between Russian stores and those of capitalistic countries is due only in part to the fact that the Russians underestimate some of their costs. The remainder is due to the fact that the costs of capitalistic stores are too high from the social point of view.

In spite of some advantages resulting from the elimination of competitive wastes, the Soviet Russian marketing system was far from a complete success in the prewar period. This was due in part to peculiarities of the Soviet Russian situation and in part to difficulties inherent in the operation of any system of large-scale state marketing. In the first place, it was unfortunate that the new Soviet marketing system had to be started practically from scratch, with new principles, new facilities, and new personnel. Scarcely any of the facilities, owners, or managerial personnel of the former system of private trading were suitable for the new state marketing system, and the development of the new meant the liquidation of the old.

Again, it was unfortunate that the foundations of the new marketing system had to be laid in a period when conditions elsewhere in the economy required the rationing of consumers' goods. Under rationing the new personnel developed the habit merely of distributing goods to depersonalized ration card holders instead of selling them to customers who could buy goods freely in any store on the basis of prices, quality, and service. This difficulty went all

the way back to the central headquarters of the marketing system where distribution plans were made on the basis of an abstract average consumer. All too often the real consumer was forced to behave like the average consumer, take what was given to him, and accept goods that he did not want in order to acquire those that he did want. And the store managers, since they did not have to worry about the tastes and needs of the real consumers under rationing, were careless about accepting defective and substandard goods from the manufacturing industries.

Soviet Russian marketing suffered also because, in spite of the difficulties present in the field, the Russian planners did not see fit to devote large quantities of effort, funds, and managerial ability to its development. The really large investments of funds and managerial talent occurred in other phases of economic activity, such as heavy industry. It was inevitable probably, with a general shortage of capital and managerial ability, that some fields of activity should be slighted, but the result was unfortunate from the point of view of retail trade. Stores continued to be relatively few in number, and they were often inadequately staffed and poorly managed. In any case, however, it was at the retail level that the problems created by the Russian government's economic policies came to a head. Large investments in heavy industry and rapidly expanding production of capital goods in a backward economy were bound to create relative shortages of consumers' goods, and the resulting dissatisfaction and distrust on the part of the people was exposed in their attitudes with regard to the stores and their struggles to get a share of the available limited goods.

Finally, it may be questioned whether merchandising (and especially the retailing phase) is as well suited to large-scale management by the government as is, for example, heavy manufacturing industry. If retailing requires quick decisions, flexibility, and ingenuity on the part of store managers, the operation of retail stores on a tremendous scale by the government is almost bound to be awkward, cumbersome, and inefficient. Thus, in the Russian system small errors at general headquarters would deprive whole areas of certain types of goods or create artificial shortages in some stores, though others in the same area were well supplied. Seasonal goods would arrive after the season was over, or would be sent to the wrong places. Supplies of goods sent to the stores were sometimes poorly adapted to local tastes and customs, and goods would pile up

on the shelves in some sections of the country while unsatisfied demands for the same products would exist in other areas.

If the government set the price of a good too low, the Russian consumers, with their distrust of the stores which had developed from long sad experience, would rush in and buy up the entire stock of the good before the government got around to change its price. If the price of a good was inadvertently set too high, large stocks of it would be "frozen" in the stores and tie up large sums of capital funds before the appropriate governmental agency got around to reduce the price. Lastly, store managers, with little chance for personal gain from the operation of their establishments and under pressure to achieve the planned volume of turnover, were sometimes reluctant to stock new types of goods because these products might move slowly and reduce store turnover. The problem of getting individual initiative and responsibility on the part of management in a government-owned marketing system proved a difficult one.

*Marketing Developments during and after World War II.* The Russian marketing system, like other phases of the country's economic activities, suffered severe losses during World War II. It is reported, for example, that 216,700 shops and stores, or well over half the prewar total, were destroyed during the war.<sup>20</sup> However, the most striking feature of the war period was the overwhelming shortage of things to sell. In July, 1941, soon after the beginning of the war with Germany, it became necessary to reintroduce card rationing of bread, butter, meat, tobacco, shoes, clothing, and other goods in Moscow, Leningrad, and other centers of population. Rationing was soon extended to the rest of the country. Some of the early war rations, such as those of meat, macaroni, and fish, were considerably more generous than those which had prevailed in the earlier rationing period, but other rations, such as those of sugar and bread, were almost identical with those of the earlier period. In the fall of 1941, the ordinary industrial worker in Moscow was receiving monthly rations of 1.5 kilograms of sugar (one kilogram = 2.2 pounds), 2.2 kilograms of meat, 2 kilograms of flour or macaroni, 2.4 kilograms of bread, 0.8 kilogram of butter, and 1 kilogram of fish.<sup>21</sup>

<sup>20</sup> *Soviet Russia Today*, May, 1948, p. 15.

<sup>21</sup> *The New York Times*, September 21, 1941.

As the war wore on, some of the rations had to be tightened a bit. In 1946, it was reported that an office worker in Moscow received a little over a pound of bread per day, and for a month 2 pounds of sugar,  $1\frac{3}{4}$  pounds of fat,  $4\frac{1}{2}$  pounds of grits or macaroni, and  $4\frac{1}{4}$  pounds of meat or fish.<sup>22</sup> Still later, in November, 1947, it was said that the top Soviet ration, for heavy workers, amounted to only 2340 calories per day. Growing children received 1114 calories and dependents 892. The average for the whole population was about 1500.<sup>23</sup> In the war period, as in the earlier rationing period, consumers were divided into several classes for rationing purposes, and different rations were assigned to each class.

The prices of all sorts of goods sold in the stores were, of course, still under strict governmental control during the war period, but prices nevertheless increased very rapidly. After the end of the war, the prices of many goods were ten or fifteen times as high as in the prewar period.<sup>24</sup> An American correspondent in Moscow reported that, at the official rate of exchange between rubles and dollars, half-soles for a pair of shoes cost \$19, an ice cream bar \$1.20, a bottle of beer \$2.25, eggs 90 cents each, milk 80 cents a quart, an ordinary nickel chocolate bar \$2.50, and sugar \$12 a pound, in 1946.<sup>25</sup> Another report stated that, in 1946, a pair of men's leather shoes sold in the commercial stores (where goods were sold on an unrated basis as in the earlier rationing period) for from 810 to 1600 rubles and an ordinary dress brought from 1500 to 2200 rubles, while the average worker's monthly wage ran less than 500 rubles. These prices reflected Soviet Russian production in 1946 of about one quarter of a pair of shoes and 9.5 meters of cotton cloth per citizen.<sup>26</sup> Apparently, the Soviet government decided, in the war and early postwar period as in earlier years, to use rising prices as a means of bringing the large total of money wages paid out to Russian workers into adjustment with the very limited supplies of consumable goods turned out by Soviet industry.

Although some price decreases were made earlier, including general cuts in food prices ranging from 63 per cent for white flour to 10 to 15 per cent for meats at the commercial stores in 1946, it was not until December, 1947, that anything could be done about ra-

<sup>22</sup> *The Champaign Urbana (Ill.) News Gazette*, October 8, 1946.

<sup>23</sup> *Time*, November 17, 1947, p. 34.

<sup>24</sup> *The Champaign-Urbana (Ill.) News Gazette*, December 15, 1947.

<sup>25</sup> *Ibid.*, October 8, 1946.

<sup>26</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 42.

tioning in Soviet Russia. At that time, coincident with a revaluation of the ruble and issue of new rubles for old in such a fashion as to relieve the citizens of practically all their hoarded cash and a large part of their bank deposits, the rationing of all food and industrial goods was ended. Prices went back to a unified system once more, instead of having separate and widely varying sets of prices at ration and commercial stores. At the same time some changes in prices were announced. The price of bread was cut 12 per cent under the old ration price. Prices of cereals and macaroni were slashed 10 per cent. Meats, fish, fats, sugar, confectionery, salt, potatoes, and vegetables remained at their old ration prices, while the prices of tea, milk and some other items were increased.<sup>27</sup> In 1948, however, it was reported that Russian consumers were still caught in a tight squeeze between food prices two or three times as high as prewar and earnings that had fallen far short of keeping pace.<sup>28</sup>

### QUESTIONS

- 1 "The organization of exchange activities under capitalism is ordinarily left rather completely in the hands of private individuals and firms." Explain.
- 2 "The prices at which economic goods are exchanged under capitalism are determined by the operation of demand and supply forces in the market and not by governmental action." Show whether you agree.
- 3 "Many activities of the federal government in the United States affect the prices of economic goods directly or indirectly." Explain.
- 4 "General price control by the government under capitalism is more likely to stabilize the official indexes of prices than it is to hold the real cost of living of the citizens at a constant level." Do you agree? Explain.
- 5 "The rationing of goods by physical quantities is no more efficient than rationing on the basis of price movements, but it is certain to result in an equitable division of scarce commodities among the citizens." Show whether you agree.
- 6 "The transition from capitalism to socialism, as the latter system is visualized in theory, would not alter exchange activities greatly." Do you agree? Explain.
- 7 "Governmental control over the prices of particular economic goods and over the level of prices in general would be inevitable under socialism." Show whether you agree.

<sup>27</sup> *The Champaign Urbana (Ill.) News Gazette* December 16, 1947.

<sup>28</sup> *Ibid.*, February 19, 1948.

- 8 Does the program of modern socialism call for widespread rationing of consumers' goods by physical quantities? Explain
- 9 "The actual range of consumption choices would be greater for most individuals under socialism than under capitalism" Show whether you agree
- 10 "Exchange activities would be extremely simple under communism" Explain
- 11 Describe the development of state marketing in the Soviet Russian economy
- 12 What is the relative importance of cooperative and governmental stores in the Soviet Russian marketing system?
- 13 What have been the chief problems in the distribution of finished goods to consumers in Soviet Russia?
- 14 What were the chief effects of the rationing of consumers' goods in Soviet Russia under the First and Second Five-Year Plans?
- 15 "In spite of governmental price control, the general price level moved upward significantly under the Five-Year Plans through 1940" Explain
- 16 "Economic goods often appear scarcer under a system of rationing by physical quantities than under a system in which the apportionment of goods among consumers occurs on the basis of price changes" Show whether you agree
- 17 "The rationing system in Soviet Russia led to very inefficient retailing" Why?
- 18 What accomplishments would be credited to the Soviet Russian system of government-controlled marketing through 1940? Explain
- 19 "The Soviet Russian system of large-scale state marketing was not a great success in the period from 1928 through 1940" Do you agree? Explain
- 20 "The Soviet Russian experience indicates that marketing is a field in which governmental ownership and operation is not likely to be highly successful" Show whether you agree
- 21 How does the present Soviet Russian marketing system compare with that which exists in the United States? Indicate both similarities and differences
- 22 What were the chief developments in the marketing system of Soviet Russia during World War II and in the immediate postwar years? Explain

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## CHAPTER 12

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### THE MECHANISM OF EXCHANGE

(Continued)

#### *Exchange Activities in Britain under Partial Socialism*

EXCHANGE activities constitute another segment of British economic life in which the basic enterprises are privately owned and operated but the activities of these enterprises are rather strictly controlled through governmental interference and regulation. As in the United States during the war period, the organization of enterprises in the field may be anything which their private owners desire, and the influence of the government is exercised through such devices as price control and rationing.

**Price Control in Britain** Great Britain, like other countries which participated in World War II, found that wartime shortages of goods available for sale, in combination with unusually large quantities of purchasing power in the hands of the citizens, required the operation of a system of price control if runaway inflation were to be forestalled. The British system of price control, however, was considerably less comprehensive than those used by a number of other countries. Prices of essential foods and many other so-called utility goods were kept low through a strong system of price control supported by the liberal use of subsidies, but that was about all. From mid-1941 on through the war period, according to the official story, the cost of living was stabilized at about 30 per cent above the pre-war level.<sup>1</sup> However, it was widely admitted that this increase in the cost-of-living index did not reflect the full actual increase in the cost of living, which was thought to be more nearly in the neighborhood of 50 per cent. And, of course, the use of rather large

<sup>1</sup> *Labor and Industry in Britain*, September October 1947 pp. 198-199

subsidies to keep prices from rising really only shifted increases in the cost of living from the consumers to the taxpayers, instead of achieving genuine stabilization.

In the postwar period, the Labor Government has merely continued the system of price control which was already in effect. The cost-of-living index rose a couple more points by the middle of 1947, and a new index of retail prices which was introduced at that time had risen by 4 per cent by the end of 1947.<sup>2</sup> The government made it clear that the cost of subsidies, which had reached £400 million, must be lowered, and it started to permit price rises for certain commodities, including even basic foods like bacon or tea, where the subsidy had been high. In the case of nonessential commodities, or those whose supply is difficult to control, prices have been left quite uncontrolled. The government has also followed a policy of deliberately increasing the prices of some commodities, by means of a heavy purchase tax or increased excise duties, in order to absorb some of the excess purchasing power of the citizens or to control the consumption of the commodities. The purchase tax on fur coats, for example, is 100 per cent. Again, through increased excise taxes, the price of a pack of cigarettes was raised from 47 to 67 cents in April, 1947, in order to curtail smoking, which plays a considerable part in connection with British expenditures of dollars. The new policy of stabilizing wages, announced in February, 1948, seems to imply much more strict control of prices in the immediate future.

*Rationing in Britain.* During the war period, Britain, like other countries, found it desirable to resort to physical quantity rationing in the case of many commodities as the fairest means of sharing very limited supplies. Since the war, the Labor Government has found it impossible to do away with rationing. The industrial production of consumers' goods has recovered sharply in many lines in the postwar period, but the need to export large quantities of some items has restricted the amounts available for domestic consumption. Nevertheless, the quantities available for consumption have increased considerably from wartime levels, and in some cases have been running in excess of prewar supplies, as the data in Table 13 show. The case of foods has been something else again. In spite of increases in agricultural production at home, Britain has remained dependent on foreign sources of supply for large amounts of food, and her continuing crisis with respect to international trade and the

<sup>2</sup> *Labor and Industry in Britain*, March, 1948, pp. 43, 44.

**TABLE 13**  
**HOME CIVILIAN SUPPLIES OF SELECTED  
 CONSUMERS' GOODS IN BRITAIN**

(Monthly averages)

Item	Prewar	1946	Late 1947
Wool blankets (thousands)	550	449	502
Footwear (million pairs)	10.7	8.9	11.2
Clocks (thousands)	400	154	361
Table cutlery (thousands)	2000	830	881
Cycles (thousands)	134	83.1	84.2
Radios (thousands)	145	78	171

SOURCE: *Statistics on Britain's Position*, February, 1948, p. 28

balance of payments has led the Labor Government on several occasions to revise downward imports, including foods. As a result, many essential foods remain in short supply, as shown by the data in Table 14.

Britain's rationing program, as of early 1948, was extremely severe for a peacetime situation. Milk, sugar, fats, potatoes, tea, and bread were rationed in specific weekly quantities (bread and

**TABLE 14**  
**FOOD CONSUMPTION IN BRITAIN**  
 (Weekly averages in thousands of tons)

Item	1938	1942	Late 1947
Flour	78.7	93.4	97.0
Rice	1.85	1.65	0.18
Sugar	40.6	28.4	31.5
Fresh and frozen meat	40.5	32.2	31.5
Bacon and ham	10.40	7.85	3.46
Fish (filleted weight)	8.80	5.33	12.87
Butter	9.65	3.18	4.82
Cheese	3.62	5.71	4.00
Eggs	8.6	4.8	4.2
Potatoes	58.6	83.8	138.4
Dried fruit	3.25	3.70	2.92
Tea	4.37	3.48	3.26
Coffee	1.96	2.53	2.55
Milk—liquid sales	72.0	92.9	105.2
Milk—used for manufacture	36.3	12.9	4.8

SOURCE: *Statistics on Britain's Position*, February, 1948, p. 27

flour rationing was finally eliminated in late July, 1948) The meat allowance had just been cut from 24 to 20 cents' worth per person per week, and the bacon ration from two ounces to one ounce. The egg ration was about one a week per person, and the non-priority milk ration was two pints a week. Children, adolescents, invalids and expectant mothers had special priorities for milk, eggs, and citrus fruits. Workers in heavy industries were allowed extra rations.

Shoes, almost all clothing, and household supplies made of textiles were rationed, the chief exceptions being hats, belts, pocket books, suspenders, umbrellas, and some heavy textiles. Clothing rationing was especially severe. If a man bought one suit and an overcoat, he would have had only enough left of his yearly coupons to acquire two pairs of socks. If a woman bought a coat, a woolen dress, a pair of shoes, and two pairs of stockings, she had only enough coupons left to buy one blouse. All nonessential driving of automobiles had been suspended and the small basic ration of gasoline, which had been restored to all the people after the war, had been abolished in mid-1947.<sup>8</sup> We may suppose that the rationing of goods by physical quantities is not intended to be a permanent feature of Britain's postwar system of partial socialism, but price control of some sort will presumably have to be retained if the operation of the entire economic system is to proceed according to the economic plans.

### *Exchange Activities under Fascism*

**The Category Corporations in Italy** Except for the control organizations at the top, little needs to be said about the organization of exchange or marketing activities in Fascist Italy. The Italian marketing system contained middlemen and retail stores of all the usual types. The marketing enterprises could be organized as single enterprises, partnerships, corporations, or cooperative associations. With the exception of governmental monopolies in the sale of such articles as salt and tobacco, the Italian government did not own and operate enterprises in the marketing field. Italian

<sup>8</sup> *Labor and Industry in Britain*, March, 1948, p. 13 and *Fifty Facts About Britain's Economic Position* New York: British Information Services, 1947, pp. 14-15. The rationing of clothing was eliminated in the spring of 1949, but without much benefit to ordinary people, who now found that they had to restrain from buying because prices were so high rather than, as formerly, because they were short of coupons.

marketing activities, however, like other phases of productive activity, came under the category corporations which were set up in 1931. No separate corporations were established for marketing activities. Six of the 22 corporations dealt with enterprises established for the performance of services, but six represented branches of economic activity which involved agricultural, industrial, and *commercial* operations while the other ten represented branches of economic activity involving industrial and *commercial* operations only. Thus, marketing activities were brought under the corporations which were in charge of form production in the various fields by giving a few representatives to the enterprises engaged in trading in the various products. For example, in the clothing corporation, there were four workers' and four employers' representatives of enterprises which marketed and traded in clothing products, the grain corporation included three workers' and three employers' representatives of firms which engaged in the grain trade, and so on. In the early days, when the corporations operated more or less as business pressure groups, some of their propositions and suggestions to the government concerned commercial activities. Later, the degree of governmental control over commercial activities through the corporations became as great as the control over form-production activities themselves.

**Control Organizations in Germany** As was true in the case of Italy, the basic organizations of German marketing under fascism were similar to those of any modern capitalistic economy. There were all the familiar general types of middlemen, and retail stores of all the usual types existed. The enterprises in marketing could be single proprietorships, partnerships, corporations, or cooperative associations, and combinations of marketing enterprises were permitted. In relation to the organizations for governmental control which were superimposed upon the German economy under National Socialism, the enterprises in the general field of marketing were under the supervision of the Estate of Industry and Trade and the National Group for Trade, which was one of six such National Groups. The National Group for Trade was divided into Economic Groups, such as Wholesale Trade and Retail Trade, and the Economic Groups were divided into Branch Groups, each of which was composed of the dealers in specific products or classes of products.

Trade activities were also represented in the National Economic Chamber, the Provincial Economic Chambers, the local Chambers

of Industry and Commerce, and the Cooperative Council of Chambers of Industry and Commerce At the top, control over marketing activities was exercised by the Minister of Economic Affairs and, in the wartime situation, by the General Council for the War Economy On the whole, trade activities were controlled to about the same extent and in about the same ways as those of industry, and there seems to be no need to repeat here the discussion which was presented in Chapter 8

*Price Control in Italy* Italy under fascism flitted with price control on a number of occasions prior to her entry into World War II in 1940 In 1927 when the stabilization of the lira at about 19 to the dollar made its value in terms of gold and foreign currencies somewhat higher than its domestic purchasing power in terms of wages and prices, Italian goods became costly from the point of view of foreign buyers, and the effect on Italy's export trade was disastrous The deflation of domestic prices seemed necessary and the government undertook, through a series of decrees, to produce a general reduction in prices, wages, rents, interest rates, and taxes in order to reduce production costs and bring Italian prices back into adjustment with the world price structure

In 1934, prices had started to rise again and a campaign was undertaken to keep the prices of commodities in line with wages Early in the year, the government established maximum prices for 21 basic commodities, most of which were foods The Fascist Party, the Federation of Merchants, and the new category corporations had charge of enforcing these maximum prices Late in 1935 when recovery from the depression and the war with Ethiopia brought further upward pressure to bear on prices, the government set up a Central Price Committee, composed of cabinet ministers, representatives of confederations, and other officials, to give Italy a central unified system of price control The Committee dealt primarily with articles of mass consumption and left the prices of other things, and especially luxury goods, unregulated

In October, 1936, Italy devalued the lira by 40.94 per cent with the idea of stimulating Italian exports and tourist trade The devaluation made it necessary for the Central Price Committee to redouble its efforts to control prices, and it required a report on all prices as of September, 1936, intending to stabilize prices as nearly as possible at the levels prevailing at that time Rents and some public utility rates were completely blocked, the prices of basic

foods were allowed to rise very slightly, and those of other consumers' goods were permitted to rise somewhat more. As before, the prices of luxury goods were unregulated.

The work of price control was turned over to the Central Corporate Committee (described in Chapter 8) by a decree of April, 1937, and the category corporations, the provincial corporate committees, and several specialised technical commissions were to serve as advisory and administrative agencies. Price controls were to be used to protect the purchasing power of the masses and to assist with the program for economic self-sufficiency. During all these experiments with price control after 1934, prices continued to rise, sometimes slowly and sometimes rapidly. Apparently even governmental price control could not resist the pressures which resulted from the shortage of goods occasioned by active preparation for war and the pursuit of self-sufficiency.

Soon after the entry of Italy into the war, the government undertook to block retail prices at the levels prevailing in June, 1940. The prefects of the various provinces were instructed to enforce the observance of the decree which forbade retail price advances. The Ministry of Corporations, to facilitate surveillance by the fiscal police, specified the exact margins of overhead and profit allowable to retailers in connection with the marketing of many important products. Store operators had to be able to show proof of the actual wholesale invoice costs of their inventories, adding only transportation and packing expense and the turnover tax. Dealers who obtained greater margins than those allowed were subject to severe penalties. The margins for store operators were fixed uniformly for all enterprises of a certain type, large or small. They did not take into consideration the varying operating costs of individual dealers or the losses which some retail establishments would inevitably make.<sup>4</sup> The blocking of retail prices was extended for the duration of the war by a decree of March 29, 1941. Later in 1941, an attempt was made to strengthen the mechanism for price control and the government created a Central Committee for the Coordination and Control of the Prices of Foodstuffs of Primary Necessity, under the chairmanship of the Secretary of the Fascist Party. The new Committee was to list foodstuffs of broad consumption, fix their prices, and arrange the prices in national and local groups. It had the power to stabilize and adjust national prices by provinces and local

<sup>4</sup> *Foreign Commerce Weekly*, March 8, 1941, p. 899.

prices by zones, to control national stocks of foods in order to perfect their distribution, and to standardize qualities and types of goods.<sup>5</sup>

**Price Control in Germany** The specific control of prices was a continuing policy of the National Socialist regime in Germany. Rising prices and wages would have enabled certain desired economic adjustments to be made more easily than they actually were, but the Nazi leaders apparently did not dare to permit an open devaluation of the mark. Besides, rising prices would have increased the difficulty of maintaining or increasing German exports, they would have added to the money costs of the armaments program and to governmental expenditures in general, and they might have increased, instead of restricting, the demand for limited supplies of tangible goods because of the fear of extreme inflation. Rising prices for industrial goods would have menaced governmental attempts to help the farmers. Moreover, fixed low wage rates are an easy and rather efficient device for limiting consumption and may have the effect of increasing the supply of labor on the market, in that more members of families may offer themselves for employment and regular workers may be induced to put in longer hours in order to get greater total wages.

Price control under National Socialism began with a decree of 1933 which prohibited increases in the prices of commodities used in public works projects. Since there was no general governmental agency for price control at the time, the enforcement of the decree was placed in the hands of the cartels or business combinations. The prohibition against price increases was expanded to include all necessities of life on May 16, 1934, and before the end of the year to include all commodities and commercial services except those controlled by the Reich Food Estate and the Chamber of Culture, or approved for inland shipping by the Minister of Transport. Despite the prohibition of price increases and the closing of some stores for violations, price indexes continued to rise slowly but steadily, and in November, 1934, a Commissioner for Price Supervision was appointed by Hitler. All cartels had to notify the Commissioner of new price agreements and restrictions and to secure his approval for all increases in prices. The Commissioner was to prevent unfair competition, which included the charging of prices which were out of line with those of normally conducted enterprises and which had no

<sup>5</sup> *Foreign Commerce Weekly*, August 23, 1931, p. 11.

relation to costs He also had to approve any price agreements or uniform bidding in connection with public contracts and enforce special price instructions relating to goods whose prices were affected by foreign trade transactions

Although the powers of the Commissioner were more effective in some fields than in others, his work was done fairly satisfactorily on the whole, and conditions were so stable that the office of the Commissioner was abolished in July, 1935 In 1936, German prices began to move upward again, partly under the influence of increases in the world prices of raw materials, and price control was difficult in the absence of any central agency Moreover, the Second Four-Year Plan was announced in 1936, and the carrying out of this plan for national economic self-sufficiency was certain to cause shortages and bring pressure to bear upon prices Therefore, the decree which provided for this plan also provided for the appointment of a national Price Commissioner, whose power would cover the prices of all commodities and services Herr Hitler duly appointed the Price Commissioner and placed him under the administration of the Four-Year Plan All other offices and agencies with partial powers for controlling prices were placed under the supervision of the Commissioner

The first action of the Commissioner, Herr Wagner, was to issue the drastic decree of November 26, 1936 which blocked the prices of all commodities and services as of the levels that had prevailed on October 18, 1936 After the date of the decree, all price increases were illegal unless approved by the Commissioner Corporations and other business enterprises could fix, agree upon, or change prices (to the disadvantage of consumers) only with the approval of the Commissioner Similarly, producers and dealers could fix or change retail prices to the disadvantage of consumers only with the Commissioner's approval Changes in credit or delivery conditions to the disadvantage of purchasers were prohibited as hidden increases in prices Finally, no price-fixing agreement on the part of cartels or other associations could remain in effect more than three years without reapplying for the approval of the Commissioner

The system of price control thus provided for seemed rather rigid at first glance, but actually there were several elements of flexibility in the system Prices that had fallen since October 17, 1936 could be raised again without permission but not above the level of October 17 In the case of falling costs, or even quite arbitrarily, the

Commissioner could decree lower prices for specific articles Price reductions of 5 to 10 per cent were made in this way for electrical equipment, chemical goods, and clocks and watches, 25 per cent for artificial fertilizers, 9 per cent for staple fiber 8 per cent for aluminum, and 10 per cent for flat glass These reductions brought savings to consumers amounting to 0 1 per cent of total retail expenditures<sup>c</sup> In the third place, the Commissioner could grant price increases in specific cases, if such increases were necessary to the firms' existence, and the need for adjustment was not the result of obvious inefficiency or an over-generous wage policy

Finally, under a decree of July 15, 1937, maximum prices for imported products were set at the level of actual cost plus economically justifiable expenses and profits Margins of cost and profit were blocked at the level of the average absolute mark-ups prevailing in 1936, so that they would not increase as the foreign prices of imported goods rose Replacement cost rather than actual cost might be used, upon the decision of the Commissioner, in the case of imported commodities whose prices were quoted on organized exchanges In similar fashion, it was provided that the prices of commodities made wholly or partly from imported materials could be varied with changes in the prices paid for these materials, though expense and profit margins could not be increased Such flexibility was necessary in the case of imported goods or commodities made from imported materials since the German government was not in a position to control the prices of goods produced in other countries

The price-stop decree was extended by the War Emergency Act of 1939 In addition to some important provisions affecting the wages, hours, and working conditions of German labor, the Act declared that all prices and price calculations should be reexamined Prices could not be adjusted because of war risks, though they could be changed on the basis of actual increases in costs, and certain war taxes could be included in prices In an attempt to secure efficiency, the principle of uniform prices for each industry was set up, with prices in general at the level of the average costs of all the firms except those subsidized by the government Governmental subsidies, incidentally, were given to firms producing important commodities under especially disadvantageous cost conditions

*Fascist Experiences with Price Control* In spite of all the efforts that were made, general price control was not a very great success

<sup>c</sup> M. Y. Sweeny, *The Structure of the Nazi Economy*, p. 100

in either fascist country. In Italy, prices moved upward rather strongly in the period before World War II. They remained most difficult to control in the war period, although repeated attempts were made to strengthen the mechanism for price control and Mussolini, like a modern King Canute, frequently rose up and commanded the tide of rising prices to stand back. In Germany, when the price-stop decree of November, 1936, was issued, it was intended that subsequent increases in prices should be very limited in number. Actually the Price Commissioner's office was swamped with complaints and requests for price adjustments, and many of the requests were granted. In fact the Commissioner stated that he had permitted adjustments freely in cases in which they seemed to be justified. The price level continued to move upward, though slowly. Over the entire period from 1933 to April, 1941, the index of wholesale prices in general rose from 90.7 (1913 = 100) to 111.9, while the index for the wholesale prices of consumers' goods rose from 109.2 to 147.3.<sup>7</sup> In the later years of the war, prices were not kept perfectly stable, but they were controlled to such an extent that inflation was not one of the major difficulties of the period, at least in so far as the official indexes of prices were concerned.

The reason that price control is judged to have been rather unsuccessful in Germany as well as in Italy is found in the difference which existed between official indexes of prices or cost of living and the real cost of living as experienced by consumers. Quite apart from any permitted increases in prices, there were innumerable direct violations of the maximum prices which had been established and black market dealings flourished. The dealers on the black market were sometimes ordinary retailers who were willing to take the chances involved in selling part of their wares to favored or prosperous customers who were not averse to paying extremely high prices for extra quantities of goods. In fact the retailers were almost compelled to violate the law in order to exist, since they were lost in a maze of regulations and red tape and since they were caught in a squeeze between fixed retail prices and rising costs of doing business. They used two faced price tags or never seemed to find time to place official price tags on their goods, and the prices actually charged were often well in excess of the legal maximum.

<sup>7</sup> F. L. Neumann, *Behemoth: The Structure and Practice of National Socialism*, p. 311.

prices In other cases, the black market operators were fly-by-night dealers created by the emergency situation

The black market violations continued despite the use of secret fiscal police to make purchases in the shops and the severe penalties, ranging up to life imprisonment or death, for violations The penal ties and attempts at rigorous enforcement merely made the black market prices higher Wartime reports from the fascist countries told of shoe laces selling at \$4 a pair, coffee at \$18 a pound, eggs at \$2 16 a dozen, butter and chicken at \$1 a pound, olive oil at \$1 per half-pint, chocolate at \$6 80 per pound, and a pound of tea or a whole ham for \$25 <sup>6</sup> Such prices paid in black markets are never taken into account in figuring official indexes of prices or cost of living

Besides the permitted increases in prices and the direct violations, there were many devices which fascist producers and business men used to feather their nests within the price-control scheme One thing which was difficult to prevent was the combination sale This device is illustrated by the case of the German farmer and his dog The farmer raised and sold hogs When any one approached him to purchase a hog, he would charge only the legal maximum price, but would make no sale unless the customer also purchased his dog Shortly after the sale was consummated and the dog was set at liberty by his purchaser, he would return to his former owner and hold himself in readiness for sale with the next hog The effect was, of course, to give the farmer more than the maximum price for his hogs

When, as in Italy at times, some prices were controlled but others were not, the business man could assure himself of a neat profit by refusing to sell a quantity of a commodity whose price was blocked unless the purchaser also acquired a quantity of some other article for which a highly profitable unblocked price could be charged In Germany, where all prices were supposed to be controlled, the margin of gain might be much greater on one commodity than on another, and the business man would refuse to sell a quantity of an article on which his profit was small unless the purchaser bought a quantity of another article on which the profit was larger Such combination sales were not regarded as cricket by the fascist authorities but the difficulties involved in preventing them were great, espe

<sup>6</sup> *The Chicago Tribune*, May 18, 1942

cially in cases in which the buyers of merchandise were quite willing to engage in them.

When the prices of all commodities and services were supposedly fixed as in Germany, it is still clear that they could not be fixed as of a given date for commodities which did not exist at the time. As a result, manufacturers were tempted to alter their old standardized products to some extent so that they would become "new" products which were not subject to the old maximum prices. Then, when the price-control agency got around to set a maximum price on a "new" product of this kind, the manufacturer would make another minor alteration and create still another "new" product, and so on. Needless to say, the new products were sold at highly profitable prices until they too came under control. Of course, the fascist authorities tried to control this practice, and it was decreed that all substitute and new products had to be registered and have approved prices placed on them before they could be sold. Manufacturers were required to submit data on the composition of the product and on its use or uses, as well as on prices and costs and the methods of their calculation. Still it was not always possible to keep business men from gaining by altering their wares.

Combinations and cartels were often able to get along very well under the controlled prices. They had formerly maintained fixed list-prices but had allowed varying discounts from these prices in periods of prosperity and depression. After prices were controlled, they received price increases in effect by merely charging the full list-prices. This practice was forbidden, but it was difficult to prevent when buyers were willing to connive with sellers. Again, the German consumers found that they had to pay higher prices than formerly even though all prices were blocked, for the producers found that high-priced goods, often of a luxury character, could be produced with a greater margin of profit than low-priced staple articles. As the staple qualities of goods at low prices disappeared from the market, consumers either had to buy better goods at high prices or go without the goods altogether. Clearly it is no boon to the consumer to have the price of low-grade shoes fixed at \$3, if, when he goes to the store to make a purchase, he finds he must buy a higher-grade shoe at \$6 or acquire no shoes.

Even under controlled prices, price increases could be obtained in effect by lowering the quality of the merchandise which was produced and sold. Clearly, a producer might profit as much by selling

an article of lower quality for the stable price of a good of better quality as by selling a good of the old quality for a higher price. In the fascist countries, decreases in quality by as much as 30 or 40 per cent were observed in articles sold at stable prices. Such decreases in quality were usually not approved by the fascist authorities, but they were rather difficult to detect and prevent in many cases. When goods were sold by the "package," rather than by definite units of weight and measure, producers could sometimes obtain a concealed price increase by reducing the contents of the package without changing the price or quality of the product. And, if all other methods failed, it was difficult to keep a purchaser from paying only the legal maximum price for a good and then wagering 100 marks or lire that the seller could not jump over his own waste basket.

Some, if not all, of these practices and resulting difficulties in enforcement are likely to appear whenever a system of stringent governmental price control is superimposed on an economic system in which productive wealth is privately owned and the actual operation of industry and business is in the hands of profit-seeking private individuals. It should be noted that all the practices studied tend to increase the cost of maintaining a scale of living composed of commodities and services of given quantity and quality, while none of the practices tends to cause even a minor flurry in the official indexes of prices or cost of living. Wherever such practices are widespread, the success of price control cannot be measured accurately by the official price or cost-of-living indexes.

Apart from the question of open or concealed violations, price control in the fascist countries produced some problems and unexpected results. Price control cannot be aimed solely at the achievement of stable prices, for price inter-relationships are also important. In Germany, for example, the farmers were once found to be feeding grain, which was needed for human consumption, to their livestock because the Price Commissioner had fixed the price of grain below that of fodder. At another time, when the government decided that the price of rye had to be raised for the benefit of the farmers but without any increases in the prices of products for consumers, enterprises in brewing, flour-milling, and other fields were placed under severe handicaps. Under a system of price control accompanied by rationing, it was found that purchasers were likely to buy all the goods to which they were entitled and to hoard them.

if they were not needed immediately for consumption Finally, price control required the calculation of costs in thousands of enterprises, trades, and industries, correspondence between governmental agencies and business enterprises concerning thousands of disputes over real costs and nationally justified prices, and the issuance of innumerable decrees and instructions by the government

*The Rationing of Consumers' Goods under Fascism* While rationing of an informal sort, through compulsory pooling of articles for sale, "guided consumption," and purchase licenses, had existed in the earlier years of fascism, formal and official rationing of consumers' goods began with the entrance of the fascist countries into World War II Long before the war was over, the rations of most goods had become extremely limited In Italy, even the initial ration of the important alimentary pastes, including macaroni and spaghetti, was only 4 4 pounds per person each month, or about a third of normal consumption<sup>9</sup> The bread ration was eventually cut so low that the ordinary consumer could enjoy only the equivalent of three one-ounce rolls of dark gray bread daily Meat was severely rationed both by means of meatless days (sometimes as many as five or six per week) and by quantity, with the allowance for a meat-day amounting to 30 to 100 grams In this connection, meat was taken to mean fresh beef, veal, pork, mutton, and goat Salt pork, bacon, and game could be served on meatless days, and poultry was sometimes available, although at one time it could be sold only on one day per week

By February, 1943, or about six months before Italy was knocked out of the war, it was estimated that the diet of the Italian light worker had taken a drop in calories of 45 per cent (67 in fats and oils, 42 in carbohydrates, and 37 in proteins)<sup>10</sup> However, the rationing program was by no means confined to foods, for clothing, shoes, leather goods of all kinds, rugs, needles and thread, pots and pans, all machines and tools, fuels, and a whole host of other things, were included in the program The fuel situation got so tight that the Italian consumers were allowed to heat their homes only for a period of forty days, or from, say, December 10 to January 19, each winter And that much house-heating, even in sunny Italy, was far from enough for comfort

<sup>9</sup> *Fascism in Action*, p. 163

<sup>10</sup> *Ibid*

In Germany, supplies of food were somewhat more adequate, and yet rations dwindled considerably as the war went on. The meat ration fell to a pound per week or less. Coffee was rationed at two ounces per month and later replaced by substitutes. The egg ration was down to 2 per month, and the butter ration to 2 ounces per week. Conditions were much the same in the case of other consumers' goods. Clothing was severely rationed by means of cards and a "point" system, and quality deteriorated rapidly. Overcoats could be purchased only if worn-out overcoats were turned in. The shoe situation was desperate. People were urged to lay aside their leather shoes in the late spring and summer and use wooden shoes until fall. There were no ration cards for shoes, but an individual was permitted to buy new shoes only if he could furnish proof that his old shoes were worn out completely and beyond repair. Shoes were resoled with artificial rubber, for there was no leather available for the purpose. Each man was allowed one three-ounce stick of shaving soap every four months—a ration which produced a temporary boom in the sale of electric razors. To the great dismay of at least a part of the population, the sales of women's hats were discontinued.

Tobacco rations were extremely limited. Men with ration cards could obtain only two or three cigarettes or one small cigar daily, and women over 25 years of age were placed on half rations. Store keepers were forbidden to exhibit in their show windows any goods which were not on sale in normal amounts within the stores. Formerly the storekeepers had been made to keep their windows decorated with samples of scarce goods to give the impression that these goods were still available. Restaurants were compelled to serve a *feldkueche*, or one-dish field kitchen meal, on two days per week. Hotels in the large cities were forbidden to rent rooms for office purposes or keep guests for more than three weeks at a time. The fuel situation was so bad that only one heated room per family could be maintained during the winter months, and some people had been trying to get around the restrictions on house-heating by living in warm hotel rooms.

Even short rations did not tell the entire story. As the self-sufficiency program substituted ersatz products more and more commonly for the natural products, the quality of many consumers' goods declined considerably. Moreover, it was often impossible to obtain certain consumers' goods at all, whether the goods were

rationed or unrationed, whether the potential customers for rationed goods had unused cards or coupons, and whether the goods were produced by natural or artificial means. Long before the end of the war, some 80 per cent of all production for civilian consumption had been stopped, and it was difficult to find in the stores such common articles as shoe laces, toothpaste, buttons, thread, envelopes, paper, paper clips, dust cloths, suspenders, floor wax, light cords, typewriter ribbons, or photographic films.<sup>11</sup>

### QUESTIONS

- 1 Indicate the nature and results of price control in Britain during the war and early postwar periods.
- 2 "The Labor Government of Britain has endeavored to hold some prices down and push others up." Explain.
- 3 "In spite of increased production, Britain has been unable to abandon the rationing of many types of goods in the postwar period." Explain.
- 4 "The Labor Government of Britain has merely carried over the wartime system of rationing into the postwar period." Show whether you agree.
- 5 How were exchange activities subjected to governmental control in Italy under fascism?
- 6 "Exchange activities were under strict governmental control in Germany under fascism." Explain.
- 7 "Fascist Italy followed a fluctuating policy with regard to price control." Explain.
- 8 Why did the government of Germany under fascism attempt to maintain strict control over the general price level?
- 9 Describe the system of price control which operated in Germany after 1936.
- 10 "Governmental price control was extremely effective in Italy under fascism." Do you agree? Explain.
- 11 How effective was governmental price control in Germany under fascism? Explain.
- 12 "Fascist producers and business men devised many methods for getting around the systems of price control in Germany and Italy." Explain.
- 13 "Price control in the fascist countries stabilized the official indexes of prices rather than the actual cost of living of the citizens." Show whether you agree.
- 14 "The rationing of consumers' goods was extremely severe in Italy and Germany under fascism." Explain.

<sup>11</sup> *The Chicago Tribune*, May 18, 1942.



## CHAPTER 13



### ***CREDIT, BANKING, AND INVESTMENT***

IN passing from commercial to financial economic activities, we may note again that there are some general principles in the new field which are valid for any type of economic system. Commercial credit, for example, must exist in any economic system which makes use of modern roundabout methods of production. With the productive processes spread over time and carried on to a great extent in anticipation of demand, there is no way to make the incurring of all expenses or costs of production and the receipt of income from sales of finished products coincide in time. Many costs must be paid some time before receipts are available from sales. In the interim, someone must extend commercial credit, that is, give up goods in the present and get them (or some equivalent value) back at some future time. Such extensions of commercial credit may or may not involve the existence and operation of commercial banks and other credit institutions. Sellers of raw materials, for example, might be made to deliver their commodities to manufacturers and wait until finished products had been produced, sold, and paid for before receiving payment for their materials. Or the central government might undertake to finance all such transactions directly. As a matter of fact, commercial credit could and would be used even in an economic system which did not make use of money.

In every economic system, indirect production, which makes use of large quantities of capital goods, is more efficient than direct production in most types of productive activity. But capital goods can be used only if "capital" is saved and invested. Saving requires the existence of surplus income over and above the bare subsistence needs of the people as consumers. From the point of view of money, individuals must not consume their entire incomes, but must save and invest a portion, if capital goods are to be created. From the physical point of view, a part of the agents of production at the

disposal of society must be taken away from the production of consumers' goods and services and must be directed into the production of capital goods. In any economy with fixed quantities of productive agents, the cost of creating greater quantities of capital goods is found in the necessity of going without, for the present, the quantities of consumers' goods and services which could have been produced with those productive agents which are actually devoted to the creation of capital goods. The cost of capital goods, in other words, is found in the necessity of abstaining from consumption to some extent.

The use of capital goods in production clearly involves the existence of investment credit. Capital goods, such as machines, are produced and delivered to the user as of a particular time but they give off their benefits over an extended period of time and not all at once. Someone must be responsible for financing the production of capital goods and for waiting a long time to receive the benefits which the capital goods can create. This function is performed by the "savers" of the economic system. There may be great differences from one economy to another with regard to the specific methods and practices used in connection with investment credit. An American corporation may obtain its investment credit by selling bonds, which must be paid off with interest, through an investment banker who is an authority unto himself as to whether the funds should or should not be extended to the company. A Russian enterprise may receive a non-repayable grant of long-term funds, which bear no interest, from a governmental bank which extends the funds merely as a part of the plan for the whole economy and without any discretion as to whether the funds should be extended or as to the amount which should be given. Underneath these surface differences, the simple fact is that there is no way in which factories and machines can be constructed and made to yield all their benefits or products immediately. Someone must advance funds or economic goods and wait for their return. Investment credit, like commercial credit, does not depend on the existence of specific types of banks or other credit institutions, or even on the use of money in the economy.

### *Credit, Banking, and Investment under Capitalism*

**Commercial Credit and Banking under Capitalism.** In a capitalistic system, a great part of the commercial credit in use is ordinarily

extended by commercial banks, though some is put out by other institutions or directly between business enterprises or between business enterprises and their final customers. The commercial banks are usually privately owned, and operated for profit, though they are often subjected to a large amount of governmental interference and control. Although the government does not usually own and operate commercial banks, it is likely to operate institutions for the purposes of central banking, of which purposes one is the supervision and control of the privately owned and operated commercial banks. The government may also own and operate certain types of credit institutions which private interests either do not furnish at all or provide in insufficient quantities.

In the United States, much of the commercial credit is furnished by the roughly 14,200 commercial banks in the country. About 6900 of these banks are members of the Federal Reserve System and the rest are state-chartered banks. The latter banks are subject only to such control and regulation as the laws of the various states provide, but the banks which are members of the Federal Reserve System are controlled rather strictly by various requirements for membership in the system and prescriptions as to methods and practices which may be employed. However, the banks are owned privately and operate for profit, and the total volume of commercial credit in existence is that which results more or less automatically from the operations of the commercial bankers.

From the social point of view, the proper role of commercial credit in a capitalistic economy is a neutral one. Commercial credit is a useful instrument for facilitating the making and carrying out of economic decisions which it would be in the interest of society to make and carry out even if commercial credit had never been invented. But commercial credit should never be allowed to affect the content and volume of these decisions and activities. That is, commercial credit should not be issued in such amounts or in such ways as will cause prices to rise, profits to increase, production to expand, and the over-extension of productive facilities to take place, so that a boom period leading inevitably to depression is created. In similar fashion, the contraction of commercial credit should not be a leading factor making for business contraction and depression. Commercial credit should adapt itself to whatever volume of economic activity is generated in the economic system. It is intended to be a lubricant rather than a prime mover.

Commercial credit, as extended by the commercial banks of the country, has never been able to live up to this ideal in the United States. That is, the total volume of commercial credit has not remained closely adjusted to the changing volume of economic activity in the country, but has shown a tendency to over-expand in periods of prosperity and to over-contract in periods of depression. It has therefore played a leading part in intensifying and prolonging these periods. Through a succession of laws, the federal government has attempted to provide methods for controlling the expansion and contraction of the total volume of commercial credit. These methods, which operate through the Federal Reserve System, now include raising and lowering the rediscount rates, engaging in open-market operations, increasing and decreasing the reserve requirements behind demand deposits, controlling margin requirements and loans on securities, and granting or withholding the use of the credit facilities of the Federal Reserve Banks to member banks according to whether they make proper or improper use of bank credit. There is no doubt that the use of these devices is able to influence the total volume of commercial credit, but they do not give the government or the central banking authorities the power to decide that the total volume of commercial credit in use in the United States at a particular time shall be so many dollars' worth and no more. The total volume of commercial credit still depends to a significant extent upon the decisions and actions of individual bankers. In this connection, it is noteworthy that, when the government wanted to control the price level in the emergency created by World War II, it resorted to a system of direct price control and did not depend on the powers of the Federal Reserve System for regulating the total volume of commercial credit and indirectly the price level.

While the total volume of commercial credit is partly under governmental control, the distribution of commercial credit among the business and industrial enterprises of the country is almost wholly independent of such control. The commercial bankers perform the function of distributing commercial credit among enterprises and industries on the basis of economic motivation and prospective profits, and not according to some plan which takes social need or desirability into account. Under ideal conditions of course, the firms which could bid most effectively for commercial credit would also be those whose products were most needed from a social point of

view, but in actual practice many firms may be good credit risks because of the ready sale of their products even though the products are far from being indispensable to social welfare.

**Investment Credit and Banking under Capitalism** In a capitalistic system, large amounts of savings are made by individuals on the basis of the relationship between interest rates and other prices. The necessary condition for such savings is that the interest rate be sufficient to overcome the time preference of the savers, or their rather natural desire to consume their incomes at present instead of in the future. However, many units of savings are quite independent of the interest rate. In this class are savings made to provide for various financial emergencies, or "rainy days," to provide for one's old age, to provide for heirs and dependents, or to obtain the power which the accumulation of large means may bring. Again, persons with very large incomes may save almost automatically because of the difficulties involved in finding sufficient consumptive uses for their incomes. Other savings, such as those which result when corporations reinvest their earnings instead of paying dividends to the stockholders, presumably depend on prospective earnings but not on the voluntary decisions of the individuals whose funds are being saved. Finally, various governmental units sometimes collect taxes from the citizens and use the revenue directly or indirectly for capital purposes. In such cases, of course, the individual citizens are not able to decide whether to save or how much to save, for these decisions are made for them.

When individuals save, for whatever reason, they may invest their savings directly in productive facilities or in the securities of corporations which will use the funds for the same purpose. On the other hand, the individual savers may place their funds in savings accounts, insurance policies, or other uses, in which cases the funds ordinarily find their way indirectly into investments in productive facilities. With large numbers of scattered savers and firms desirous of obtaining funds for investment purposes, there is clearly a need for some type of intermediary or go-between to bring the savers and borrowers together. This function is performed to a large extent by investment bankers in a capitalistic system such as that of the United States. Individual enterprisers and partners must depend largely upon their own wealth and savings, upon direct loans from other persons or institutions with funds to invest, and upon the reinvestment of their earnings, in satisfying their needs for long-term capital.

funds. Moreover, corporations do not use the services of investment bankers when they reinvest their earnings or engage in attempts to sell their securities directly to the individual savers. But corporations obtain large quantities of long-term capital funds by selling their securities with the assistance of the investment bankers.

Investment bankers handle security issues for governmental units as well as for corporations and intend to serve merely as intermediaries for bringing together the business and governmental institutions which desire long-term funds and the individuals and institutions which have these funds to invest. The investment bankers do not expect, if all goes well, to tie up their own funds for very long in the security issues which they sell. By performing their functions of investigation, underwriting, and distribution, the investment bankers eventually get the governmental and business securities into the hands of insurance companies, banks, and investment trusts, corporations seeking investment for surplus funds or accumulating a sinking fund, and individual investors.

From the social point of view, the things which we should desire from our investment banking system may be readily stated. First, the system should provide the greatest possible degree of safety for the purchasers of securities. That is, they should be protected from securities that are fraudulent in character and from security salesmen who greatly overstate the possibilities of the securities which they sell to the investing public. In the second place, investment banking should be carried on efficiently and in a manner consistent with the public welfare. This general requirement in turn means three things: (1) the volume of investment credit should not be so greatly expanded at certain times and restricted at others that its issuance becomes an important cumulative factor in causing business instability; (2) the total volume of investment credit must be distributed among the industries seeking it in such a way that the creation of new productive facilities will be coordinated with the desires of consumers for finished products; (3) investment banks, in performing their functions, should not be allowed to get a strangle-hold on industry by threatening to withhold needed credit if such control should be denied them.

Without going into great detail, it may be said that the investment-credit system of the United States has fallen well short of perfection with respect to all these matters. Sellers of securities have frequently been more optimistic as to the future of their stocks

and bonds than the situation has warranted, and many of the securities sold to the public have turned out to be worthless or almost worthless. It is estimated that American purchasers lost some 25 billion dollars on valueless securities purchased in the boom period preceding 1929. The total volume of investment credit has not been well adapted to the changing needs of the economy. The investment banking business has operated by fits and starts. In boom periods, investment credit comes out in a veritable flood, and at other times it dries up to a mere trickle. At times, the volume of new investment credit has been in excess of the total volume of current savings available for investment, since commercial banks have lent funds to customers to permit them to buy securities on what amounted to an installment plan. At other times, the total volume of new investment credit has fallen far short of current savings, and saved funds have lain idle in the banks. There is little doubt that the operation of our investment credit system has contributed to business instability.

The distribution of investment credit among firms and industries by profit-seeking investment bankers has not brought a close coordination with society's needs in all cases. Under ideal conditions, to be sure, the firms and industries whose securities were most attractive to the investment bankers from the point of view of making money would also be those firms and industries whose productive facilities needed most to be expanded from the point of view of consumers' needs for finished products. In practice, however, the pursuit of profits may lead to the direction of funds into the construction of new palaces for the very rich, instead of the building of model apartments for workers, even though the rich are already magnificently housed and the workers are living in slums.

Finally, investment bankers have required sometimes a degree of control over corporate affairs as a condition of issuing investment credit. Such control may be achieved by having a corporation appoint one or more members of the banking firm to its board of directors, ostensibly for the purpose of looking after the safety of the security issues. A few years ago, it was reported that one investment house in this country, together with its dependents and allies, was represented by directorships in corporations with net assets of some 74 billion dollars, or about one-fourth of the total of American corporate assets at the time. This power was held by some 167 representatives of the banking house who, in turn, held some 2450 inter-

locking directorships in corporations<sup>1</sup> More recently, the National Resources Committee reported on various "interest groups" which combine industrials, railroads, and public utilities with financial organizations in informal communities of interest The so called Morgan-First National interest group contained 13 industrials, 12 public utilities, 5 major railroad systems, and 5 banks The companies had total assets of over \$80,000,000,000 The second, or Kuhn-Loeb group, was composed of 5 major railroad systems, 2 other railroads, 1 utility, and 1 bank, with total assets of almost \$11,000,000,000 The smallest of 8 interest groups included companies with assets of almost \$2,000,000,000<sup>2</sup> In such cases, it is suspected that investment banking houses exercise control powers far beyond those which are necessary and appropriate to the simple conduct of their own business

In this discussion, we are not suggesting that investment bankers as individuals are either worse or better than other men, or that they are personally responsible for all the shortcomings of investment banking as a phase of economic activity Indeed, a good socialist might contend that our investment bankers have behaved as well as could be expected in a capitalistic system and that the faults which have developed are in large measure chargeable to the capitalistic system itself which permits such a vital phase of economic activity to be privately owned and operated for profit We must also remember that our investment banking system has been successful in transferring tremendous quantities of capital funds from savers to enterprises and industries, that most of the uses of investment credit have been more or less desirable from the social point of view, and that the rapid capital development of the United States has been the marvel of the world

The activities of the federal government in controlling investment banking in the United States have been directed almost entirely to the problem of providing safety for investors The Securities Act of 1933 was intended to provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails and to prevent fraud in the sale thereof Issues of securities must file with the Securities and Exchange Commission registra-

<sup>1</sup> H W Lindler, *The World Tomorrow*, "Have We a Money Trust? September, 1931, pp 282-284

<sup>2</sup> National Resources Committee, *The Structure of the American Economy* Washington Government Printing Office, 1939, pp 306-317

tion statements providing all information about the securities which investors need to know. Until these statements are filed, the securities cannot be sold or offered for sale in interstate commerce or through the mails. The Act also provided for the civil liability of security issuers to investors who suffer losses, provided the registration statement, or the prospectus offered to investors, contained false information or omitted material facts. The Securities Exchange Act, passed in 1934, required the licensing of security exchanges and the registration of all security issues which are listed on the exchanges. It also defined, or gave the Securities and Exchange Commission the power to define, the functions of brokers, dealers, and specialists, and forbade certain manipulative practices on the security exchanges, under penalty of heavy fines or imprisonment, or both. The other problems in the field of investment banking have been left virtually untouched and it is difficult to see what could be done about some of them unless the investment banking industry were to be socialized.

### *Credit, Banking, and Investment under Socialism and Communism*

**Commercial Credit and Banking** The manner in which commercial credit would be extended and commercial banking would be operated in the economic system of modern socialism can be predicted in advance at least in general terms. That commercial credit would be used goes without saying. Moreover, since the functioning of commercial credit institutions is so important to all other types of enterprises and since a privately owned and operated commercial banking system could do so much to disrupt the operation of other phases of economic activity, it is unthinkable that any part of commercial banking should remain in private hands under socialism. Commercial banking would need to be taken over by the government at an early point in the process of socialization.

Under socialism, there might well be a single state bank to carry on commercial banking activities, with as many branches as would be necessary to care for all the short-term credit needs of the system. All types of firms would presumably have accounts with the state bank, and these accounts would be debited for the various expenses of the firms and credited with their receipts of money income. There is no way of knowing whether individuals would be permitted to use

the commercial banking facilities by depositing their money incomes and drawing checks to meet expenses. Each firm would probably be given an original deposit or grant of funds, in its account at the state bank, for working capital purposes. Such a grant would be expected to be large enough to cover the regular expenses of the production period. That is, enterprises would normally receive income from sales before they had entirely used up their balances at the bank in payment of operating expenses. If various types of emergency situations caused the balances of particular firms to be almost or entirely used up, these firms could borrow additional quantities of commercial credit for short periods of time from the bank. The charging of interest in connection with commercial credit might be desirable from the point of view of an accurate accounting for costs. It would make little difference from any other point of view since the government, or the people as a whole, would both own and operate most industries and furnish the funds for purposes of commercial credit. The status of an enterprise's account at the bank would indicate whether or not the enterprise was operating with planned efficiency.

Since an ideal communistic society would presumably try to operate without using any money or prices, there would be no commercial banks in such a system, either operated privately or by the government. If modern methods of roundabout production were used, commercial credit would have to exist in the sense of waiting for the future results of productive activities undertaken in the present, but no suggestion is available as to how the problem would actually be handled.

*Investment Credit and Banking.* Enterprises under socialism would require large quantities of fixed capital equipment, but whether the capital goods would actually be put through the price mechanism would remain to be determined. The capital goods could be produced in state industries and merely issued to various enterprises and industries according to plan, without any question being raised concerning the prices of such goods or the obtaining of funds with which to purchase them. On the other hand, the capital-goods industries might operate like other industries, with certain money costs to meet and certain money prices to be obtained from the sale of products. In this case, enterprises needing new capital goods would have to come into the possession of funds with which to buy them. The institutions issuing long-term capital funds

would certainly be owned and operated by the government and would give out funds as necessary for the fulfillment of the economic plans of the system rather than on the basis of the prospective profitability of the various enterprises and industries. There would seem to be no strong reason for the state to charge itself interest on funds issued to its own enterprises for long-term capital purposes or to require such funds to be paid back at some future time. Investment credit would also exist under ideal communism, since capital equipment would be produced at a particular time and it would be necessary to wait for years to get the resulting benefits. However, investment credit in such a system apparently would not make use of prices and money or banking funds.

### *Credit, Banking, and Investment in Soviet Russia*

**The Gosbank** In the socialistic system of Soviet Russia, both commercial credit and commercial banking are in use. Commercial banking is a governmental monopoly operated by the State Bank, or Gosbank, which has over 4100 branches scattered throughout the country. In addition to granting short-term or commercial credit to all types of economic enterprises and clearing accounts between these enterprises, the Gosbank has charge of the emission of currency, the receipt, holding, and disbursement of all funds under the unified national budget and local budgets, and the flotation of state loans. The affairs of the Gosbank are administered by a Council and a Board of Directors. The Council (composed of the Minister of Finance, the Board Chairman of the Gosbank and other banks, and other individuals) guides the general policy of the bank, approves important decisions, passes on the opening or closing of branches and offices, nominates the Board of Directors, and fixes the limits on specific-purpose credits, overdrafts, and current accounts. The Board of Directors of seven members has charge of the detailed operation of the bank.

In all, something like 3,000,000 enterprises have accounts at the Gosbank. All transactions between economic units or enterprises pass through the Gosbank and are paid and received by a simple debiting and crediting of accounts. Enterprises are not allowed to grant commercial credit to each other by means of book accounts, promissory notes, or any other devices. This inter-enterprise credit had been permitted at one time but it made the total amount of

credit issued difficult to control and interfered with planning.<sup>3</sup> When one enterprise buys goods from another, its account at the Gosbank is debited when it notifies the bank of its approval of the invoice for the goods or authorizes the bank by letter of credit to pay the account. The account of the selling enterprise is then credited. In earlier years, the Gosbank used to credit the seller's account before debiting that of the buyer. In addition to being an unusual accounting procedure, this practice resulted in many abuses on the part of sellers, such as filling orders with substandard goods, charging excessive prices, and disregarding delivery dates.<sup>4</sup> While all transactions between enterprises are financed through the Gosbank, the individual citizens receive their incomes in cash and do their buying and selling by means of cash, for they are not allowed to have accounts at the Gosbank.

**Grants and Loans** Every new economic enterprise which is to have an account at the Gosbank receives its original basic working capital as a grant from the bank out of budget funds. That is, the enterprise's account at the Gosbank is credited with an amount which is supposed to be sufficient to enable it to carry on all its "normal" operations without any need for borrowing. If the enterprise operates with normal efficiency, its bank account will be replenished by income from sales before it is entirely used up in connection with the payment of ordinary operating expenses. These original grants of commercial credit do not have to be repaid and bear no interest. In addition to these non-repayable grants, the Gosbank makes loans to all sorts of enterprises for the purpose of handling seasonal requirements and meeting temporary and occasional needs. These loans are made for specific purposes and are repayable at a predetermined fixed date with interest.

The Gosbank makes both planned and unplanned loans. The planned loans are those which are made to cover the values of goods in transit, to meet seasonal needs for purchasing raw materials and supplies, and to enable enterprises to carry on the seasonal processes of production.<sup>5</sup> In particular, these loans now involve production credits which are made, as additions to working capital, as goods are manufactured and finished, or bought and sold. Firms in certain

<sup>3</sup> A. Z. Arnold, *Banks, Credit, and Money in Soviet Russia*. New York: Columbia University Press 1937, pp. 345-347.

<sup>4</sup> *Ibid.*, pp. 356-358.

<sup>5</sup> *Ibid.*, p. 376.

manufacturing industries may obtain these loans up to 20 per cent of the value of incomplete manufactured goods and up to 50 per cent of the value of finished goods ready for shipment. Procurement and sales agencies may receive credits up to 50 per cent of the cost of goods handled.<sup>6</sup> The unplanned loans are made in cases in which the shipment of goods is hindered or prevented by transportation difficulties, embargoes, or the failure of purchasers to honor invoices, when the normal operations of production are disrupted by the failure to receive raw materials and supplies, or when goods are produced which were not contemplated in the economic plans or whose amounts are in excess of planned estimates.<sup>7</sup> The commercial loans of the Gosbank vary in length from 30 days to six months and bear interest at rates of 2 to 4 per cent, depending on the type of loan.

The methods of the Gosbank in extending commercial credit to economic enterprises may seem peculiar at first glance but they are actually not very different from those which are used in the United States. We often think of American enterprises as always getting their commercial credit from the commercial banks by means of loans which are repayable with interest. Actually, a new enterprise, which is just being formed and which is not yet in operation or producing anything, might experience great difficulty in obtaining its original fund of working capital by means of a short-term loan at a commercial bank in the United States. Its original funds, both for fixed and working capital, are likely to be obtained by the sale of securities if it is a corporation. To the extent that funds are obtained by the sale of stocks, they amount to a grant rather than a loan which is repayable with interest. That is, a return does not have to be paid to preferred stockholders unless it is actually earned, and even the presence of available earnings does not necessitate a payment to common stockholders. Moreover, stocks do not obligate the corporation to repay at any time the amounts which the stockholders have invested. About the only difference between the Russian and American systems is that the Russian enterprises receive their original grants of working capital from the people as a whole through the government, while American corporations receive such grants from limited groups of security purchasers. Actually operating enterprises in both systems, when they need additional funds

<sup>6</sup> *Foreign Commerce Weekly*, January 11, 1941, p. 61.

<sup>7</sup> A. Z. Arinold, *Banks, Credit, and Money in Soviet Russia*, p. 378.

for temporary and occasional purposes, go to commercial banks and obtain loans which are repayable at definite times with interest.

*Money in Soviet Russia* Actual money or cash plays a relatively unimportant part in the Russian planned economy, as it does in most capitalistic economies. Paper money and subsidiary coins are provided, in such amounts as are needed, through the Ministry of Finance and the Gosbank. Russian money is purely an internal currency, and it has been completely removed from the influence of international forces, for Russia maintains a separate monetary unit for use in the transactions in international trade, which are carried on by a governmental trading monopoly. The domestic currency is all fiduciary money and is not convertible into gold, though Russia usually has a considerable supply of gold on hand. The issue of currency is planned along with all other phases of economic activity but the quantity of money is not manipulated in order to control other phases of economic activity as is sometimes the case with the "managed currencies" of other countries. Since prices are under strict governmental control, increases in the total volume of money and credit cannot result in the bidding up of prices by any automatic process, though the planners may see fit to increase prices as the total quantity of money and credit increases. The total money in circulation in Russia increased from a little over 2 billion rubles to more than 11 billion rubles between 1928 and 1936, when the publication of statistics on money in circulation was discontinued.<sup>8</sup>

*Economic Control through the Gosbank* The Gosbank is much more than an agency for issuing commercial credit and for clearing obligations between enterprises. The administration of the bank is divided into numerous departments for the supervision of credit activities and for planning work in connection with specific branches of economic activity. In fact, the Gosbank plays an important part in connection with economic planning for it draws up a financial counterpart of the economic plans of the country in addition to keeping the individual enterprises within their financial plans. Moreover, the Gosbank keeps a constant check on the efficiency with which individual enterprises operate. The very status of an enterprise's account at the bank is an indication of its efficiency. If an enterprise is supposed to break even on its operations, its account at the bank should neither increase nor diminish. If it makes either planned or unplanned profits, its balance at the bank

<sup>8</sup> A. Yugov, *Russia's Economic Front for War and Peace*, p. 144.

will grow, but, if it operates inefficiently and sustains losses, its balance will decrease. When an enterprise's balance at the bank declines without justification, an investigation may ensue and its manager may be replaced.

The Gosbank's vigilance extends to almost all details of the operation of economic enterprises. It has insisted on standard "turnover" periods, accurate credit allowances, and the prompt repayment of loans. It attempts to control the quality and finish of manufactured goods and to obtain reductions in the quantities of defective goods produced and in the number of "mistakes" such as those involved in shipping machines with important parts missing. If a plant is irregular in its manufacturing processes, falls short of its planned quotas of finished goods, or runs its proportion of "seconds" or "rejects" too high, it can be penalized at once and brought back into line by having its supply of funds cut off or reduced. In the case of procurement and supply agencies, check-ups by the bank every week or ten days are expected to disclose any irregularities which occur in purchasing or distribution, and a curtailment of bank funds will force the agencies to use their own funds to restore their required balances.<sup>9</sup>

*Evaluation of Russian Commercial Banking.* The Russian system of commercial banking experienced some difficulties and growing pains during the early years of the planned economy. After the banks had been liquidated during the moneyless period of War Communism, it was a trying task to establish a large-scale system of commercial banking and make it operate. New enterprises in business and industry had to become accustomed gradually to bookkeeping and using their accounts at the Gosbank, and to tying in the bookkeeping with the bank accounts. The opening of hundreds of bank branches and the starting of hundreds of thousands of accounts by industrial and commercial enterprises led to almost endless confusion in the absence of a large, trained banking personnel. In many cases the banks could not even ascertain the status of their clients' accounts when claims came in for debiting and crediting. Frequent changes in the main economic plans of the country were a disruptive influence in connection with the financial plans which were constructed and operated through the Gosbank.

On the whole, however, the Gosbank and its subsidiary organizations have operated with considerable success, as is evidenced by the

<sup>9</sup> *Foreign Commerce Weekly*, January 11, 1941, p. 61.

fact that there have been no important changes in the Gosbank or its methods of operation in more than a decade. The total short-term credit extended by the Gosbank has increased steadily over the years. The system of commercial credit centering around the bank seems very well suited to the Russian planned economy. Both the total volume of money and commercial credit and its distribution among enterprises and industries are in the control of the government and the economic planners, and it should be possible in time to coordinate them closely with the general economic plans for the system. In other words, money and credit serve as lubricants of the economic machine in Russia. They are not able to interfere with planned economic development or influence the content of the planners' decisions. The results which are planned may or may not suit the wishes of the individual citizens and may or may not furnish consumers with the highest possible standards of living, but any such faults which develop will not be chargeable to the system of money and commercial credit.

*The Revaluation of the Ruble.* Although the commercial banking system undoubtedly sustained losses of facilities and personnel during World War II, on the whole it was probably less disrupted by the war than any other phase of Soviet Russia's economic activity. About the only postwar development in the field now under discussion which needs to be recorded here was the reevaluation of the ruble. During the war period large amounts of cash had been paid to the Russian citizens for their services in production, while at the same time only very limited quantities of consumers' goods had been available for them to purchase. As a result, large hoards of cash and bank deposits had been built up and continued to hang over the market for goods in the postwar period. The Soviet authorities felt that the rationing of consumers' goods could not be discontinued until a part at least of this surplus purchasing power had been destroyed. Out of the several methods which would have been available for this purpose, the reevaluation of the ruble was chosen.

On December 16, 1947, the Soviet government began to issue the new ruble currency and to convert outstanding assets into it at varying rates. Actual holdings of cash had to be brought to the banks where they were converted at the rate of one new ruble for each 10 of the old rubles. The citizens who had banked their money (at the savings banks) received one new ruble for each old one on the

first 3000 rubles of deposits, two new rubles for three old ones on the next 7000, and one new ruble for two old ones on all deposits above 10,000 rubles. Citizens who had invested their hard-earned cash in government bonds were given new bonds with a face value of one ruble for each three rubles of face value of the old bonds. At the same time, the rationing of consumers' goods was eliminated, all enterprises were directed to pay wages at the same rates in the new rubles as they had in the old, and the prices of some consumers' goods were reduced below the levels which had prevailed under rationing.

*Saving and Investment in Russia* The amazing capital development of the Soviet Russian economy under the Five-Year Plans gives ample evidence that saving and investment have gone on at a rapid rate. Decisions relating to the division of the national income as between capital goods and consumers' goods (and services) are made by the economic planners at the head of the system on the basis of general directives received from the Communist Party. The Russian system of capital accumulation makes savers out of all the citizens. As the planners decide to devote certain proportions of the available productive agents to the creation of new capital goods rather than consumers' goods and services, all the citizens of the economy save in the sense that they go without the consumers' goods and services which these productive agents could have been made to produce. In similar fashion, when the new capital goods are finished and come to enhance the productivity of the nation's industries, all the citizens share in the resulting benefits by receiving larger real incomes and higher standards of living than formerly. However, the individual citizens have for the most part no chance to decide whether to save or how much to save, on the basis of interest and other price considerations, and the total volume of saving and investment is determined by government fiat and not by the will of the citizens. Conceivably a group of planners who planned to save too much could be replaced by another group of planners who would decide to save less, but that is all.

While large-scale saving is inevitable in an economy which is aiming at a rapid capital development, there is some question in a socialist economy as to whether the resulting capital goods should be put through the money and price mechanism. The economic planners, having decided the total quantity and kinds of capital goods to be produced in a given period, could simply direct the necessary

productive agents into their production and distribute the resulting capital goods as physical items to the enterprises and industries which were to receive them. In this case, the total money income paid to workers (or any other income receivers) in the economy would be just enough to make it possible for consumers to take the available quantities of consumers' goods and services off the market. No money income would be paid out to anyone to match the production of capital goods, since individuals would not be allowed to purchase these goods in any case. On the other hand, if the capital-goods industries were to pay money costs and receive money prices for their products, it would be necessary to get large amounts of funds into the hands of the enterprises and industries which were to receive the capital goods. In this case, the total money income paid out to workers and others would be more than enough to purchase all available consumers' goods and services, and the government would proceed to recapture a part of this money income and turn it over to the enterprises and industries which were to acquire new capital goods.

*Sources of Investment Funds.* Russia has definitely decided to follow the second of these alternatives, and this is the main reason why the national income and the volume of retail trade, as stated in rubles, far outrun the total ruble value of consumers' goods produced. Having paid out a total money income which is much more than sufficient to buy all available consumers' goods and services, the government uses several means to recapture a part of it. The leading device for this purpose is the turnover tax, which is similar to a sales tax. In 1938, the tax yielded 83.3 billion rubles, or 71.4 per cent of the revenue of the federal government. It was applied at varying rates to different commodities and made up from 15 to 90 per cent of the retail prices of the goods. In the case of sugar, for example, the retail price was 4.2 rubles per kilogram, of which 3.57 rubles went for the turnover tax and only 0.63 ruble for cost of production. The tax absorbed 58.6 per cent of the total receipts of retail trade in 1938.<sup>10</sup> In 1945, the rates of the tax ranged from 5 per cent of sales price for iron and coal to 83 per cent for vodka and produced 38 per cent of total federal revenues.<sup>11</sup>

The profits tax is another source of funds for investment purposes. According to plan, many industries sell their products for

<sup>10</sup> M. T. Florinskij, *Toward an Understanding of the USSR*, pp. 165-166.

<sup>11</sup> *The Soviet Union Today*, p. 16.

prices which are more than enough to cover planned costs, and the government takes the greater part of the profits which are made. In 1940 the profits tax yielded 21.3 billion rubles or 12.0 per cent of total federal revenues. In 1945 it brought in 7 per cent of the total income taxes and other direct taxes on individuals produced 15 per cent of total revenues in 1945 and social insurance levies brought in 3 per cent. Fixed deliveries in kind from agriculture and customs levies were other important sources of income. The balance of federal revenues, 11 per cent in 1945, came from the sale of government bonds.<sup>12</sup> The bonds are sold in part to the individual citizens, who are allowed to receive income on their investments, and in part to savings banks, which must invest all their available funds in these bonds. The savings banks are operated by the government, and there were 29,000 of them in 1945. Their deposits amounted to 7.3 billion rubles and they paid 3 per cent interest on them.<sup>13</sup> The total income of the government in 1945 was over 300 billion rubles, of which some 39 billions were invested in new productive facilities.<sup>14</sup>

*Investment Banking.* The funds which the government devotes to new investments are turned over to enterprises and industries by four investment banks (and their numerous branches), all of which are owned and operated by the government and are under the Gosbank. In the first place, there is the Prombank, or Bank for Financing the Capital Construction of Industry and Electrification. It directs funds for capital construction into the enterprises of all the Ministries which have charge of producing capital goods and consumers' goods, and also into the enterprises in the Ministries of Foreign Trade, Transportation, Waterways, and Communication and under the departments of Civil Aviation, Roads, and Cinema. Until 1934, the bank made both interest-bearing, repayable loans and non-repayable grants bearing no interest. In 1934 all former loans were cancelled and the bank now makes grants exclusively. The second investment bank is the Torgbank, or Bank for Financing the Capital Construction of Trade and Cooperatives. It makes grants of funds to governmental trading enterprises but mostly loans to cooperatives. Its financing of cooperative enterprises is limited to those outside the fields of agriculture and housing.

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*, p. 48

<sup>14</sup> *Ibid.*, p. 47

The Selkhozbank, or Bank for Financing Socialist Agriculture, passes out funds for capital investments in state farms, collective farms and Machine Tractor Stations. It makes grants to the state farms and Machine Tractor Stations, but mostly long-term loans at low rates of interest to the cooperative (collective) farms. All debts incurred by collective farms before 1933 were cancelled in 1934. Finally, there is the Tzekombank, or All-Union Bank for Financing Municipal and Housing Construction. This bank has no branches, and operates through the local municipal banks. It finances (1) all housing construction except that which occurs in connection with state farms or simultaneously with the construction of industrial enterprises, (2) municipal construction involving such things as waterworks, sewers, roads, and bridges (unless these works are to serve the needs of industry or transportation exclusively), and (3) the construction of hospitals, sanatoria, educational institutions, and other institutions. Prior to 1934, it made both loans and grants. In 1934, all outstanding loans were cancelled and the bank must now make grants to governmental enterprises. All these investment banks handle both governmental funds and those which are accumulated by the enterprises in their respective fields. Besides distributing investment funds, they must supervise the construction of productive facilities, try to eliminate waste, extravagance, and unbusiness-like practices, and work for increased efficiency in capital construction.

*The Extent of Russian Capital Investments.* The capital investments of the Russian planned economy have been most impressive in terms of rubles, and, of course, have been responsible for the rapid industrialization of the economy and for the speedy mechanization of agriculture. Up to 1928, the socialized economy had made capital investments of only 26.5 billion rubles. Under the First Five-Year Plan, total capital investments amounted to 60 billion rubles and investments in the socialized sector of the economy came to some 50.5 billion rubles. The latter investments considerably exceeded the planned estimate of 46.9 billion rubles. The Second Five-Year Plan called for capital investments of 133.4 billion rubles, while the actual investments amounted to 114.7 billion rubles. Capital investments under the Third Five-Year Plan were to amount to 188.2 billion rubles, and the Soviet economy was well along toward the realization of this goal by the end of 1940.<sup>16</sup> The Fourth Five-

<sup>16</sup> A. Bajkov, *The Development of the Soviet Economic System*, p. 421.

Year Plan (1946-50) calls for total investment of 250 3 billion rubles in the socialized sector of the economy.<sup>16</sup>

*Evaluation of Russian Capital Investments* We have no criticisms to make of the mechanism by means of which capital investments are made in Russia, for this mechanism seems both suitable and more or less inevitable in a socialized economy. Decisions as to the total quantity of saving and investment and as to the distribution of capital funds and capital goods among enterprises and industries are made by the planners at the head of the system and not on the basis of the market mechanism. There is no way of determining in advance whether or not the results of these decisions will be better suited to the needs and desires of the individual citizens and of the economy as a whole than are the results achieved under capitalism. All we know is that the results achieved in Russia are based on a consideration of social need, in so far as the planners are able to determine social need, and are not those which come more or less automatically from the pursuit of profits by private investment bankers. The other problems associated with investment credit and banking under capitalism can scarcely arise in the Russian planned economy. All the citizens are "investors" in the national economy and there can hardly be any question of protecting them against fraudulent or overvalued securities, or shady manipulative practices. The same high authorities which plan saving and investment are those which, in the name of the people, own and operate the enterprises which receive capital funds and capital goods. Thus, there is no problem of the extent to which investment bankers control the enterprises and industries which they help to finance.

The results of the Russian program of capital investment may be criticized from several angles. In the first place, the Russian investments have been very costly. Inefficiency and low productivity of labor were just as common in the construction of productive facilities as in other phases of productive activity, and the new productive facilities and capital goods often cost much more than had been planned. Thus, while plans for the ruble value of new capital investments have been quite well fulfilled on the whole, the actual physical quantities of productive facilities and capital goods obtained have usually been well under the planned estimates. Much of the capital construction and building has been of low quality in spite of high cost, and the Russian authorities are given to including

<sup>16</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 21.

large amounts of unfinished productive facilities in their estimates of accomplishment in the field of capital construction

Russian capital construction has also been afflicted by "gigantomania" or the delusion that, if an ordinary large-scale plant is desirable and efficient, a plant many times as large must be still more desirable and efficient. For example, in setting up an electric heat-and-power station for the Moscow area, the plans called for an enormous plant with a capacity of 200,000 kilowatts. Construction began in 1932, but the station was still unfinished at the end of the Second Five-Year Plan in 1937. If the plan had provided for 8 or 10 stations of 20,000 or 25,000 kilowatts each, some of the stations at least could have been completed and in operation by 1937. Again, it is claimed that other gigantic enterprises, such as the Magnitogorsk and Kurnetsk metallurgical works and the Molotov motor works at Gorki, were too large to be managed efficiently. Then early difficulties may have been due in large measure to inexperienced and inadequately trained management, but even after years of experience the plants have not been able to increase their efficiency greatly or increase the rates of output to anything like theoretical capacity. The extremely large plants were also sometimes located far from the necessary raw materials and markets so that their operation imposed an immense burden on the transportation system. In later years, the Russian leaders have decreased the size of the new plants which have been built. Under the Third Five-Year Plan, cotton mills with 50,000 rather than 100,000 spindles, automobile plants capable of producing 50,000 rather than 200,000 cars per year, and coal mines with a capacity of 300,000 rather than 700,000 tons per year were the order of the day.<sup>17</sup>

Criticisms of the results of the Russian investment program have not come entirely from outsiders by any means. In 1938, Russian spokesmen said that the program of capital construction in the past had shown many shortcomings, such as the construction of too many separate and detached buildings, the failure to locate new plants near established enterprises, so that cooperation in matters of manufacturing, housing, transportation, and municipal services could be achieved, the over-expansion of certain types of productive facilities, the construction of temporary buildings in permanent form, the use of expensive decorative features, a lack of standardization of

<sup>17</sup> *Fortune*, July, 1941.

productive facilities, and the construction of excessively large individual plants<sup>18</sup> In the same year, the Council of Ministers decreed the formation of a Committee on Construction to set up standards concerning construction designs and execution, the use of materials and overhead costs, to confirm the standards of the various Ministries on these points, to confirm standards of cost estimates, to present prices for materials, construction, and sanitary-technical equipment to the Council of Ministers for confirmation, to present the Council of Ministers with opinions on projects and estimates suggested by others, to confirm individual type designs, to examine projects for the regional planning of centers of large industrial construction, to work out and submit measures on questions of improving and cheapening construction, and to supervise the execution of construction projects<sup>19</sup>

The Russian investment program has been weighted heavily in favor of the capital-goods industries. This does not mean merely that the Russians have been taking capital goods instead of consumers' goods, for that result is inevitable under any investment program. It means that the Russians have been concentrating on the construction of capital goods which will produce more capital goods rather than capital goods which will produce consumers' goods. The Second Five-Year Plan called for total investments of 53.4 billion rubles in heavy (capital goods) industries, as compared with 16.1 billion rubles in light industries, 15.2 billion rubles in agriculture, and 26.5 billion rubles in transportation. Under the Third Five-Year Plan, investments were to be 87.2 billion rubles in heavy industries, 16.4 billion rubles in light industries, 18.0 billion rubles in agriculture, and 35.8 billion rubles in transportation.<sup>20</sup> Such investment programs imposed great hardships on the consumers of the Russian economy. Moreover, when low efficiency and high cost made it necessary either to fall short of planned goals in connection with the investment program or to impose further sacrifices on the consumers of the system, the Russian leaders never hesitated to select the latter alternative. Under the Second Five-Year Plan, for example, investments in heavy industries amounted to 49.8 billion rubles or over 93 per cent of the planned amount,

<sup>18</sup> *Russian Economic Notes*, Number 364, pp. 1-3.

<sup>19</sup> *Ibid.*, pp. 1-3.

<sup>20</sup> A. Bilykov, *The Development of the Soviet Economic System*, p. 421.

while investments in consumers' goods industries were only 8.8 billion rubles, or less than 55 per cent of the planned amount.<sup>21</sup>

Outside observers have often questioned the judgment of the Russian leaders in connection with some of the projects of the investment program.<sup>22</sup> Under the first two Five Year Plans, for example, several billion rubles were invested in agricultural machinery and equipment, but the increase in the gross value of agricultural production over the period probably would not have paid maintenance and replacement costs on the machinery and equipment, without raising any question of obtaining a return on the investments themselves. Critics suggest that it would have been better to make some of these investments in cotton textile machinery rather than in farm machinery, since cotton textiles were always extremely scarce and the machinery in use was inadequate for the processing of current crops. Again, the Russians have constructed enormous hydroelectric plants which even the rapidly growing industries of the country could never use nearly to capacity in the past. Critics suggest that it would have been better to use part of the funds to create badly needed housing facilities for the people.

It is clear that the Russians have been trying, as someone has said, to "starve through to future greatness."<sup>23</sup> In view of the plight of the Russian consumers and the fact that Russian productive facilities still fall far short of those of leading industrial countries such as the United States, it is clear that this future greatness is still to be attained. Every economy should have a healthy regard for future as well as present productivity and welfare, but unbalanced emphasis on the future may be just as unfortunate as unbalanced emphasis on the present, for too great a neglect of consumers' wants in the present may endanger future productivity and welfare. Moreover, when a country goes all out for a capital-investment program, there is always a question as to how useful the enormous quantities of productive facilities are going to be in the future in view of probable changes in technology and in human wants.

These criticisms should be considered as qualifying but not destroying the gains which Russia has received from her investment program. Certainly, Russia has experienced a very rapid capital development. It is commonly estimated that Russia, under the

<sup>21</sup> *Ibid.*

<sup>22</sup> L. L. Hubbard, *Soviet Trade and Distribution*, pp. 313-316.

<sup>23</sup> B. Brutkus, *Economic Planning in Soviet Russia*, p. 226.

planned economy, has been taking about a third of her national income, on the average, in the form of new productive facilities. This is a rate of capital development which would be difficult to match in any other country. The large investment program may not have been (and still may not be) well suited to the collective will of the people, but it has given the planners a large part of what they wanted and of what they thought the people and the country needed. As a matter of fact, Russia needed every scrap of her newly developed productive facilities in the struggle with Germany. If the planners had decided to give the Russian people more consumers' goods and fewer productive facilities in the past, the people might have regretted that decision bitterly long before now.

In this connection we may note that the Russian planners have done well in the last decade in decentralizing their productive facilities and scattering them over the country. Not so many years ago practically all Russian manufacturing industries were located in the Leningrad-Moscow-Ukraine area, only 300 to 500 miles from the Western frontier. More recently, facilities for the production of oil, coal, iron and steel, automobiles, looms, chemicals, copper, and many types of machinery have been located in Siberia and the Ural Mountain region. Such locations are sometimes 1300, 2000, or even 3000 miles from the Western boundaries of the country. In all, the share of the Leningrad-Moscow-Ukraine area in the industrial production of the country was reduced from 90 per cent to 60 per cent even before the war.<sup>24</sup> The Fourth Five-Year Plan continues this emphasis on decentralization of industry.

#### QUESTIONS

- 1 Why are both commercial and investment credit necessary in any economic system which makes use of modern productive methods? Explain.
- 2 To what extent does the federal government control the issuance of commercial credit in the United States?
- 3 "From the social point of view, the proper role of commercial credit in a capitalistic economy is a neutral one." Explain.
- 4 How are funds for investment-credit purposes transferred from the hands of savers to those of industrial firms in our capitalistic system?
- 5 To what extent does our investment credit system produce the results which are desired of it from a social point of view?

<sup>24</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 152.

- 6 'The activities of the federal government in the United States in controlling investment banking have been directed almost entirely to the problem of providing safety for investors' Show whether you agree
- 7 Describe the probable operation of commercial and investment banking under modern socialism
- 8 Describe the operations of the Gosbank in extending commercial credit in Soviet Russia
- 9 How are "grants" and "loans" used in connection with commercial credit in Soviet Russia?
- 10 Differentiate between the manner in which an enterprise in Soviet Russia gets its original credit at the Gosbank and the manner in which it gets subsequent credits there
- 11 "Individual firms obtain both original and additional amounts of working capital in about the same way in both Soviet Russia and the United States" Do you agree? Explain
- 12 Compare the commercial credit mechanism of Soviet Russia with that of the United States, indicating both similarities and differences
- 13 "The Gosbank of Soviet Russia is much more than an agency for issuing commercial credit and for clearing obligations between enterprises" Explain
- 14 Evaluate the Soviet Russian system of commercial banking as it operated in the period before 1940
- 15 Why was it necessary to revalue the Russian ruble after the end of World War II, and how was this revaluation accomplished?
- 16 What are the two alternatives open to the government of Soviet Russia in handling the problem of investment and capital formation? Explain
- 17 How does the Soviet Russian government obtain its funds for investment credit purposes? How are these funds distributed to industrial and other enterprises?
- 18 "The results of the Soviet Russian program of capital investment in the period from 1928 through 1940 may be criticized from several angles' Explain
- 19 'In giving the Russian people many new productive facilities and relatively few consumers' goods in the past, the Russian planners may have made a wise decision even though the citizens would have chosen differently if they had had an opportunity' Explain

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CHAPTER 14

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**CREDIT, BANKING, AND INVESTMENT**  
*(Continued)*

*Credit, Banking, and Investment in Britain under  
Partial Socialism*

**Commercial Banking** As we noted in an earlier section, the Bank of England has been brought under governmental ownership and operation, but this does not mean that banking as a whole has been nationalized. The thirteen large joint-stock banks with their almost 10,000 branches continue to operate under private ownership and management. There is no doubt, however, about the power of the Labor Government to control commercial banking in Britain. The Bank of England always had great influence with the commercial banks of the country, both through moral suasion and through the use of the customary central banking devices and techniques. These informal powers of the Bank have been made formal and permanent. That is, the Bank has been given statutory powers to obtain information from and make recommendations to the other banks, if this appears necessary or desirable in the public interest. If authorized by the Treasury, the Bank may issue directions to insure that its requests for information will be met and its recommendations will be carried out. In this way the Government's control can extend to such matters as the total amount of credit to be issued by the commercial banks and its allocation among industries and businesses.

**Investment Banking** In the field of investment credit and banking there is also no doubt about the power of the Labor Government to exercise control. Under the Banking Control and Guarantees Act of July, 1946, the Government has the power to regulate all new access to the capital market and to establish in this matter the pri-

orities which are deemed essential in the national interest. The Act also empowered the Treasury to guarantee long-term loans made to facilitate industrial development, particularly when a depression threatens. Both of these measures are related also to the Government's cheap money policy, which has lowered interest rates considerably for all types of loans.

The government's program of capital investment was set forth in broad terms in its *Economic Survey for 1947* which gave the percentage of total expenditure that was to be devoted to new housing, industrial building, the equipment of various types of industry, the development of roads, canals, harbors, and railways, and other purposes. In the middle of the year, total capital investment was running at a rate of about £1550 million a year, and a rate of £1600 million was forecast for 1948. Later in 1947, however, the continuing crisis in regard to international trade and foreign exchange led the government to curtail its much needed program of housing construction, in order to save on expenditures for foreign lumber, and to make a large cut in capital expenditures for the reequipment and modernization of British industry. On the other hand, the government decreed that the latter cut in capital expenditures should not apply in agriculture or the vital coal industry.

The total investment of £1600 million originally planned for 1948 would have represented about 20 per cent of the estimated gross national product.<sup>1</sup> Such a rate of investment, while large, would not have been out of line with what other important industrial nations are doing. The *Economic Survey for 1948*, issued in March, called for total investments of £1420 million during the calendar year, and a year-end rate of £1320 million per year.<sup>2</sup> In the field of housing construction, special efforts were to be made to speed up the finishing of houses, while cutting the total number under construction. At the end of 1947, some 100,000 new houses had been loosened and were waiting completion. As forecast in 1947, the cut in the program of capital investment was expected to affect industrial investment very heavily, because of the need for large amounts of steel in industrial construction and reequipment. The limited resources which could still be made available in this field were to be directed to those projects which would make the most substantial and early contribution to increased exports and the reduction of

<sup>1</sup> *Economic Survey for 1948*, p. 38.

<sup>2</sup> *Ibid.*, p. 39.

essential imports. Clearly, the government has the power to control both the total amount of investment credit in Britain and its allocation among industries and businesses.

### *Credit, Banking, and Investment under Fascism*

**Governmental Organizations for the Control of Banking** When the category corporations were set up in Italy in 1934, banking activities were placed in the third group, which consisted of corporations representing enterprises established for the performance of services. More specifically, banking and insurance activities were lumped together in the Corporation of Credit and Insurance. This corporation was composed of

A president and 52 members, including representatives of the Fascist Party (3), Ordinary Credit Institutions (2), Provincial Banking Institutions (1), Financial Institutions (1), Private Bankers (1), Foreign Exchange Dealers (1), Stock Brokers (1), Bank Executives (1), Bank Employees (7), Foreign Exchange Dealers' Employees (1), Ordinary Savings Banks (4), Public Credit Institutions subject to the supervision of the Finance Ministry (2), Agricultural Credit Institutions (1), "Monti di Pieta"—public pawnbrokers (2), Public Credit Institutions' Employees (3), People's Cooperative Banks (1), Agricultural Banks (1), Employees of People's and Agricultural Banks (2), Private Insurance Companies (2), Insurance Company Executives (1), Employees of Insurance Companies (3), Insurance Agents (1), Insurance Agents' Employees (1), Employees of Public Insurance Institutions (1), Mutual Insurance Enterprises (1), The Governor of the Bank of Italy (1), The President of the Industrial Reconstruction Institute (1), The President of the Istituto Mobiliare Italiano (1), The President of the Association of Italian Joint Stock Companies (1), The President of the National Insurance Institute (1), The President of the National Fascist Institute of Social Insurance (1), The President of the National Fascist Accident Insurance Institute (1).<sup>3</sup>

The Corporation of Credit and Insurance operated in much the same fashion as the other category corporations which we have described in previous chapters.

Banking activities in Germany also found their place in the regular organizational scheme for the control of economic affairs in general. Banking was one of the six National Groups under the Estate of Industry and Trade, the National Economic Chamber, the Ministry of Economic Affairs, and the General Council for the War

<sup>3</sup> W. G. Weil, *Fascist Economic Policy*, p. 116. Reprinted by permission of the President and Fellows of Harvard College.

Economy Like the other National Groups, that for banking was divided into a number of Economic Groups and Branch Groups. Bankers were also represented in Provincial Economic Chambers, local Chambers of Industry and Commerce, and the Cooperative Council of Chambers of Industry and Commerce, and were subject to the influence of these organizations.

*The Regulation of Commercial Banking in Italy.* The Italian banking system consisted of the Bank of Italy (the central bank), three "national interest banks" whose operations through branches covered the entire country, five large commercial banks known as "public law banks," and a number of small commercial and savings banks. By the decree of March 12, 1936, the Bank of Italy became a public institution and was required to give up its former commercial banking business. While it could continue to make advances on securities, both to individuals and to other banks, its discounting operations were limited strictly to commercial paper furnished by other banks. The decree required that the capital of the Bank of Italy be paid off to its private shareholders and that the new capital of the bank, amounting to 300 million lire, be subscribed to exclusively by the banks and insurance companies of the country. Thus, the Bank of Italy became a bankers' bank and a central banking institution somewhat similar to the central banks of England and the United States.

At the same time, the three large "national interest banks" (the Banca Commerciale Italiana, the Credito Italiano, and the Banco di Roma) were also made into public institutions and their stock was transformed into registered bonds which could be owned only by individuals or bodies of Italian nationality. Apparently these three institutions still did not function to the satisfaction of the fascist leaders, for the Industrial Reconstruction Institute took them over in 1939 and produced an increase from 4.2 to 9.4 billion lire in their loans to industrial and commercial firms over the next two years.<sup>4</sup>—a development which was gratifying to the fascist leaders. No change was made in the five "public law banks," for they had no stockholders, distributed no dividends, and were managed by governmental officials and representatives of local bodies.

The same decree of March, 1936, provided new controls over the operation of the commercial banks of the country. Designed for the

<sup>4</sup> Italian Library of Information, *Business and Financial Report*, January February, 1941.

protection of savings and the regulation of credit, the decree set up an office of inspection, headed by the Governor of the Bank of Italy, and gave it extensive powers of supervision over all the banks and savings institutions of the country. Its powers in connection with commercial banking included the control of interest rates on both deposits and loans and the regulation of short-term credit. It was also supposed to see to it unofficially that the savings of Italian citizens, as collected by the banks, were funneled as quickly and completely as possible into government bonds.

*The Control of Commercial Banking in Germany.* Even before the post-1929 depression, the German government was important in the banking field. The Reichs-Kredit-Gesellschaft had grown to be one of the largest institutions of the banking industry, the national government (and state governments as well) had set up a number of banks for special purposes, and the assets of public banks amounted to at least 40 per cent of the total assets of all banks. After the banking crisis of 1931, the German government controlled most of the large banks of the country. Either directly or through the Gold Discount Bank, the government owned 91 per cent of the capital stock of the Dresdner-Bank and Danat, 70 per cent of the Commerz- und Privatbank, 70 per cent of the Allgemeine Deutsche Kreditanstalt, 66.6 per cent of the Norddeutsche Kreditbank, and 35 per cent of the Deutsche Bank and Diskonto Gesellschaft.<sup>5</sup> Altogether the government controlled about 70 per cent of all German corporation banks. However, the National Socialist government of Germany soon decided against the nationalization of the banks and, over a period of a few years, returned most of the bank stock which it owned to private hands.

While German commercial banks became privately owned and operated, they were still subject to strict governmental control and supervision. The banking law of December, 1934, set up a credit supervisory board which included the president and vice-president of the Reichsbank, four secretaries of states, and a member appointed by the Chancellor of the Reich. It also created a Reich Commissioner for credit. In 1939, the supervisory board was transformed into an independent Reich control board, with a separate president and with power to act as an executive agency under the Minister of Economic Affairs in connection with all matters of credit policy. The authority of the board then extended to all banks.

<sup>5</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, pp. 30-31.

and credit institutions including even the Reichsbank and the Gold Discount Bank. The board had a licensing power which enabled it to control combinations of banks and the number of new banks and branches. Banks which seemed unnecessary under local economic conditions or whose owners and managers lacked the necessary training, experience, character, or other qualifications could be refused licenses. The board had extensive powers of audit and examination and could require the banks to furnish any needed information.

The new banking law provided detailed regulations concerning the actual extension of credit. A bank's loan to any one enterprise could not exceed a certain percentage of the bank's capital. This figure, as determined by the supervisory board, was usually 5 per cent, but it could be 10 per cent in individual cases if all partners or managing directors agreed to making a loan of this size and duly reported it to the banking authorities. Credits of over a million marks to individual concerns had to be reported to the authorities every two weeks. In making any unsecured loans of more than 5000 marks to individual customers, the banks could require full information concerning the financial affairs of the debtors and could insist upon "adjustment" for purposes of sound financing. Ostensibly, these regulations were intended to prevent banks from getting too completely tied up with individual firms, to keep several banks from making large loans to the same firms, with each bank in ignorance of the others' activities, and to compel the banks to distribute small credits among a large number of firms. Actually, however, "exceptions" to most of the regulations made it possible for large firms to get their credit needs cared for, and the regulations did not apply in any case to credits extended to the government or guaranteed by the government. The regulations did make it difficult for new firms to establish themselves or expand on the basis of bank credit. As a result, such firms had to attempt to sell securities and had to secure the government's permission to do so. The regulations had the result of directing the uses of bank credit toward ends desired by the state.<sup>6</sup>

The banking law gave the supervisory board the power to determine bank reserves. The cash reserves against all liabilities other than savings deposits, as determined by the board from time to time, could not be set at a level higher than 10 per cent. Secondary

<sup>6</sup> *Ibid.*, pp. 136-139.

reserves, which included 90-day commercial bills, treasury bonds, and public loans, could be set at any level up to 30 per cent. The banks were expected in practice to keep their secondary reserves largely in the form of bonds issued by the national, state, and local governments. The reserves of savings banks had to be kept at the banks and consisted largely of government bonds, which were more profitable to hold than cash. Needless to say, the banks, under these regulations, provided a large and ready market for government bonds, and they were active also in promoting and supporting the sale of bonds to other investors.<sup>7</sup>

Although the government gave the appearance of not interfering greatly in the ordinary daily operations of the banks, the actual position of the banker in the Nazi economy was not exactly enviable. Each banker was practically a state official as well as a private enterpriser and he was likely to have a Party man to watch over and "protect" him at all times. When instructed by the government, and without regard for his own opinions and desires, the banker had to advise his customers to purchase government bonds or the securities of new concerns which were being set up to produce *eisatz* or substitute products under the national self-sufficiency program. He was required to hold the official optimistic view of state finances. He had to try to restrain individuals who wanted to withdraw their deposits for private uses, report individuals who did make large scale withdrawals, inform the government concerning individual customers who had large liquid balances, and so on.

*The Control of Investment Credit in Italy.* Before the great depression which began in the late 1920's, investment credit and banking activities in Italy were allowed to go their own way for the most part, except that the government extended funds directly on some occasions to industries which it wished to encourage. During the financial crisis precipitated by the depression, however, the government took the long-term financing of industry and business entirely out of the hands of the banks, and entrusted it to a number of governmental institutes. After 1931, the Istituto Mobiliare Italiano made loans to industry which partly satisfied the need for funds for investment credit purposes. In January, 1938, the government established the Istituto di Ricostituzione Industriale (Industrial Reconstruction Institute) which gave financial aid to industrial firms by means of long-term loans financed through the issue of bonds guar-

<sup>7</sup> *Ibid.*, pp. 139-141.

anteed by the government. The government also increased greatly the activities of the Consorzio per Sovvenzioni su Valori Industriali, which was a government-controlled consortium, established in 1914, for industrial financing. In addition there were several other institutes or other organizations set up to operate in particular fields of industries.

A large part of the outstanding securities of Italian enterprises and industries came into the hands of these government-controlled institutions, and they were active in extending new long-term credits to the industries of the country. Since the personnel and the policies of these agencies were directly controlled by the government, another avenue for governmental control over economic activity was furnished by these financial institutions. In 1910, it was stated that the total amount invested in national economic development since 1922 had reached 22.7 billion lire. The total included almost a billion lire of direct treasury investments in the share capital of companies, some 126 million lire of special treasury advances, over 6.25 billion lire of treasury subsidies and grants, and some 5.4 billion lire of investments in land reclamation.<sup>8</sup>

The banking reforms of 1936 also affected activities in the field of investment credit, for the inspectorate which was set up had the power to supervise the issue of bonds and shares whenever issued by the credit institutions under its control, it authorized the listing of bonds and stocks on the Italian stock exchanges, it supervised the investment policies and practices of the banks, and it regulated the extension of long-term credit. Investment credit activities were also controlled by the requirement of licenses for the establishment of new industrial plants, the compulsory transformation of small corporations into other forms of business organization, the requirement that government bonds be used as security behind some corporate bonds, a 6 per cent limit on corporate dividends (later replaced by a progressive tax on dividends), a transfer supertax on the sales price of securities, and a tax on capital gains. On the whole, investment credit and banking activities were thoroughly controlled by the government.

*The Control of Investment Credit in Germany.* The National Socialist government of Germany interfered in the field of investment credit and banking in many ways. In the first place, it carried on a campaign to lower the rate of interest on long-term funds

<sup>8</sup> Italian Library of Information, *Business and Financial Report*, May, 1940.

A rate of interest of 6 to 7 per cent on such funds had been a considerable obstacle to recovery in 1933 and 1934. It operated against the borrowing of funds for long-term purposes by private firms, placed a severe burden on debtors and especially governmental units, and made it difficult for the government to convert short-term borrowing into long-term. A large part of the funds which might have supported the market for bonds was going into the repayment of loans at the banks and into the purchase of foreign securities at low prices. Savings deposits were also growing quite rapidly and savings banks at the time were not allowed to use deposits for the purchase of bonds, though this was permitted later on. The average yield on savings deposits was much lower than that on bonds, but security prices were subject to wide fluctuations and savers apparently preferred the greater security of savings deposits. Short-term investments, such as bank acceptances, treasury bills, and special government bills issued in connection with the program for employment creation, also competed for the funds which might have been used to support the bond market. However, the National Socialist government refused to lower long-term interest rates by decree or to compel the conversion of bonds bearing high interest into others with low rates of interest.

The government went to work on the problem of long-term interest rates in other ways. In 1933, municipal securities valued at 2750 million marks were converted into bonds guaranteed by the national government and bearing 4 per cent interest. Bond owners who refused to accept conversion were not allowed to obtain either principal or interest on their investments for five years. Public funds were also used to secure the conversion of farm mortgages with a reduction in interest rates from 6 to 4 per cent. Late in 1933, the Reichsbank was given the power to engage in open-market purchases of bonds and support the bond market. In 1934, the national government succeeded in converting a small bond issue with a reduction in interest from 6 per cent to 4.

A considerable disparity existed between the prices of industrial securities and those of government bonds, for the prospective earnings of industries were rather attractive under the influence of the public works program. In early 1934, the government passed a law to compel the private corporations to invest in government bonds. Any corporation which declared dividends higher than those of the

preceding year was required to invest the increase (in so far as the rate exceeded 6 per cent) in government bonds. Later in the year, the law was revised and all corporations which declared dividends of more than 6 per cent, or in some cases 8 per cent, were required to pay the surplus dividends into the Gold Discount Bank which would invest them in government bonds. Such surplus dividends were to be returned in cash in 1938. The law was extended for another three-year period in 1937 and there was a change in the provision for the return of accumulated surplus dividends. Instead of being paid back in cash, they were to be returned in the form of non-interest-bearing tax certificates which would not be accepted in payment of taxes until the 1941-45 period. In 1933, the government considered lowering the maximum dividend rate on industrial securities to 3 per cent, but finally decided against the proposal. Finally, a new law of June, 1941, prohibited all increases in dividends except for firms paying less than 6 per cent at the time. Cash dividends were limited as before, but the companies were once more to invest their surplus earnings directly in government bonds. Heavy taxes were placed on excess dividends. These taxes reduced a 7 per cent dividend rate to 6½, and an 8 per cent rate to 7, while rates higher than 8 per cent would result in an actual reduction in the dividends received by the security owners.<sup>9</sup>

The limitations on corporate dividends were intended to facilitate governmental financing and to make firms finance their long-term capital needs out of their own earnings. Low dividend rates on industrial securities increased the relative attractiveness of government bonds bearing moderate rates of interest. The program also permitted governmental control of the distribution of long-term funds among industries. Plants producing goods for ordinary civilian uses were not allowed to float new security issues and could not make earnings large enough to finance an expansion of productive facilities. Plants producing armaments and other desired goods could avoid investment in government bonds by ploughing all earnings in excess of 6 per cent back into the business. If such plants did not use their earnings for expansion but tried to pay them out as dividends, all excess dividends went to the government which could use the funds to finance any desired extensions of productive facilities. Finally, the securities of firms which could not earn the divi-

<sup>9</sup> *Foreign Commerce Weekly*, August 16, 1941, p. 6.

dends permitted by law tended to drop in price on the market, and this would have made it difficult for them to obtain new funds in any case.

Besides the policy with respect to corporate earnings and dividends, the Reichsbank induced a decline in the interest rates on short-term loans in 1933 and 1934 by lowering its own rediscountrate, and bonds could then be sold at lower interest rates than formerly. Confidence in the ability of long-term borrowers to meet their obligations gradually increased and bond prices returned nearly to the par level in 1935. At this time the government went in for large-scale conversions. Bonds valued at about ten million marks were converted at par in 1935, but with interest at 4½ per cent instead of 6 per cent.<sup>10</sup> Bond owners who accepted conversion could deduct 20 per cent of the nominal value of their bonds from tax payments owed to the government. Those who refused conversion could draw interest at the old rate but their bonds were no longer negotiable—that is, they could not be used as collateral at the Reichsbank and were no longer quoted on the Stock Exchange. The success of this scheme was overwhelming, and the government proceeded to lower long-term interest rates in similar fashion for commercial banks, states and municipalities, and on non-agricultural private mortgages. In 1940, the interest rate on savings deposits was lowered from 3 per cent to 2½ or 2⅓ per cent.

The German government was in complete control of investment credit operations, and there was no danger that it would lack funds so long as business firms or private individuals had cash or other liquid assets. Regardless of the attitude which the government might take toward the payment of its existing obligations, it could still continue to take over private funds. It could forbid the payment of private debts or arbitrarily decrease the interest on private debts and take for its own uses the funds which would otherwise have been devoted to these purposes. Savings banks, insurance companies, and municipalities were required to invest considerable portions of their liquid funds in government bonds or treasury bills. The proportion was sometimes as high as 75 per cent of liquid funds for municipalities. Even before 1938, insurance companies had to have permission from the government to make private loans even though the loans were secured by first mortgages and after

<sup>10</sup> G. Reimann, *The German Economy*, p. 164.

1938 private loans by insurance companies were entirely forbidden.<sup>11</sup>

On the whole, the national government planned to use directly something like 80 to 90 per cent of the available long-term funds, and the remainder had to go into projects which were approved by the government and Party leaders. The development of the governmental monopoly of investment funds is shown clearly by the statistics for security issues in Germany in the 1930's, as presented in Table 15. In 1928, government bonds made up only about 28 per cent of all new issues of securities, but in 1938 they amounted to

TABLE 15

*NEW ISSUES OF SECURITIES IN GERMANY IN SELECTED YEARS*

Year	<i>Government Bonds Issued (in Million Marks)</i>	<i>Industrial Bonds Issued (in Million Marks)</i>	<i>Stocks Issued (in Million Marks)</i>
1928	633	294	1339
1932	248	10	150
1933	71	2	91
1934	75	4	143
1935	1636	3	156
1936	2670	47	395
1937	3150	258	333
1938	7744	107	822

SOURCE: G. Reimann, *The Vampire Economy*, p. 165.

over 89 per cent. Naturally, the investment funds obtained by the government were used to develop only those activities which were in line with the general aims of the government. Any industries which were not essential to those aims had to finance themselves or go without funds.

Under these circumstances, the activities of German stock exchanges fell to a very low ebb under National Socialism. On the basis of tax receipts from sales on the stock exchanges, it appears that transactions on the exchanges in 1937 were only about 20 per cent of what they had been ten years before.<sup>12</sup> This result was due in large part to the drying up of security issues by private companies, but direct governmental regulation also played a part. The stock exchanges were regulated by a decree put out in March, 1934.

<sup>11</sup> *Ibid.*, p. 166.

<sup>12</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 144.

Each exchange had to obtain a charter from the national government, and the president and other members of exchange boards were appointed by the appropriate Chambers of Commerce Quotas on the exchanges were made by official brokers who were appointed and recalled by state governments All stock transactions had to be made on a cash basis, and "blocked balances" in German financial institutions could be used to purchase stocks only if they arose out of the sale of stocks Transactions by corporations in their own securities were not forbidden but had to be reported annually The number of German stock exchanges was reduced from 21 to 9 and only the larger stock issues were listed and dealt in on the exchanges For example, an issue had to have a nominal value of 1,500,000 marks in order to be listed on the Berlin exchange Since stock issues had to come out in units of 1000 marks, individuals of small means found it impossible to buy and sell them

There was a considerable amount of investment of long term funds in Germany which involved no issues of securities either by private firms or by the government That is, the government insisted frequently that industrial enterprises expand their facilities, in order to increase production, by reinvesting a part of their earnings In other cases, firms were ordered to construct dug-outs and bomb shelters, or put in lunch rooms or toilet facilities for their workers, or install large quantities of the new types of machinery which were necessary to the processing of *eisatz* raw materials The firms were often reluctant to increase their productive facilities to meet needs of an essentially temporary character, but governmental plants were likely to be established if they failed to follow orders Moreover, if the firms accumulated financial reserves and failed to keep them hidden, the government was likely to send out inspectors to look over the accounts and records of the firms If any errors or false statements were found, the firms were likely to be penalized by fines which would approximate the size of their financial reserves suspiciously well The firms were loath to operate at a rate beyond normal capacity because of increased costs and heavy wear and tear on productive facilities They never knew when they would be allowed to replace and repair their equipment In 1938, capital construction as a whole ran about 45 per cent beyond the 1929 level, but replacements were actually less than in 1929<sup>18</sup> Productive equipment in some industries was allowed to decline considerably In

<sup>18</sup> G Reimann, *The Vampire Economy*, p 139

the railroad industry, locomotives decreased in number from 250 to 222 thousand from 1929 to 1938, freight cars decreased from 660,1 to 577,1 thousand, and passenger cars from 68,2 to 61,3 thousand, in spite of a general increase in transportation needs<sup>14</sup>

Besides being required to make investments in expanding their own productive facilities, German firms with large earnings and a desire to accumulate reserves were often compelled to invest funds in new plants for quite different purposes, such as the production of ersatz materials. The Krupp firm was required to underwrite a plant for the production of artificial rubber and to furnish financial assistance to the Krupp firm in Austria, which was in the machine-tool business. The I. G. Farbenindustrie, a chemical concern, which was already helping the government by operating one plant for the production of synthetic gasoline, was once required to finance two other large plants.<sup>15</sup> When the Hermann Goering Iron Works was set up, the government furnished 270 million marks out of a total capitalization of 400 million marks. The remainder of the stock, without voting rights, was assigned arbitrarily and compulsorily to other iron and steel firms, and firms in other industries. Even the workers in some enterprises were required to buy 50 marks' worth of stock each.<sup>16</sup> This new iron and steel enterprise furnished a type of investment which established firms and private individuals would ordinarily have been anxious to avoid. It had to make use of non-ore of low quality and with too high a content of silicic acid, so that new types of blast furnaces, more coke, and other expensive changes were required. Finally, the government itself sometimes underwrote the construction of desired plants in fields which were too risky or undesirable for private investment. One such case was the construction of the productive facilities for turning out the cheap "people's automobile," a project which was never completed because of the war.

In addition to these positive requirements as to what German firms should do with their earnings, there were many types of negative interference. We have already noted the limitations on the use of earnings to pay dividends to stockholders. German firms in some industries were also forbidden to reinvest their earnings or to expand their productive facilities. In a large number of industries, the

<sup>14</sup> *Ibid.*, p. 151.

<sup>15</sup> *Ibid.*, pp. 125-129.

<sup>16</sup> *Ibid.*, pp. 129-131.

construction of entirely new plants and the establishment of new firms could not be undertaken unless permission had been obtained from the government. On the whole, the governmental control of investment credit and banking probably operated to eliminate some waste of capital and certainly kept investment funds from being used for purposes which seemed undesirable to the state. On the other hand, no definite and continuing agency, such as a national investment board, existed for the purpose of planning Germany's investments, and the uses into which the government directed investment funds probably were not well suited to the desires of the German citizens as individuals.

World War II brought one final development in the field of credit. In 1940, it was announced that the enterprises connected with the National Economic Chamber would undertake the collective guaranty of certain types of loans and credits. One such type involved the loans and credits granted by the Deutsche Industrie bank and the Bank der Deutschen Luftfahrt in connection with transactions related to the war economy and executed under the instructions of the Minister of Economic Affairs (credits required for plant expansion or re-equipment in shifting from peacetime to wartime production). The second type included emergency bank credits extended by the German Corporation for Public Works to enterprises whose liquidity was seriously impaired by the requisition or blocking of stocks of raw materials or inventories of finished products. The guaranty amounted to 100 per cent in connection with loans of the latter type but only 10 per cent for loans of the former type.<sup>17</sup>

#### QUESTIONS

- 1 "Commercial banks are still privately owned and operated in Britain under partial socialism, but the government has the power to control their activities." Show whether you agree.
- 2 How can the British government under partial socialism control the field of investment credit and banking? Explain.
- 3 Describe the Labor Government's activities in the field of capital investment in Britain in 1948.
- 4 How did the government control commercial credit operations in Italy under fascism?
- 5 How was Italian commercial banking affected by the banking reforms of 1936?

<sup>17</sup> *Foreign Commerce Weekly*, October 19, 1940, p. 106.

- 6 "The government of Germany under fascism took several steps to bring commercial banking under strict governmental control" Explain
- 7 "Each commercial banker was practically a state official as well as a private enterpriser in Germany under fascism" Show whether you agree
- 8 "Privately owned banks were virtually eliminated from participation in the long-term financing of industry in Italy under fascism" Explain
- 9 Describe the government's campaign to lower the rate of interest on long term funds in Germany under fascism
- 10 "The German government under fascism was in complete control of investment credit operations" Do you agree? Explain
- 11 "The development of the governmental monopoly of investment funds in Germany under fascism is clearly shown by the statistics for governmental and private security issues in the 1930's" Explain



## CHAPTER 15



### ***THE DISTRIBUTION OF INCOME***

Once the production of commodities and services has taken place, the next important problem in any economic system concerns the manner in which these economic goods are to be divided or apportioned among the individual consumers of the economy. The distribution of income does not refer to the processes by means of which physical goods are brought from producers to consumers, but rather it refers to the division of the national income, first in money and then in commodities and services, among the owners of the productive agents. As long as all the productive agents of an economy are incapable of producing an adequate volume of commodities and services for consumption, the question of income distribution is likely to remain in the background while attention is concentrated on the problem of increasing the total volume of production. But, as the total productive power of the economy increases, the problem of income distribution grows in relative importance. Indeed, some of the most severe criticisms which are directed at the operation of capitalistic economies at the present time deal with this very matter of the distribution of income.

#### *The Distribution of Income under Capitalism*

***The General Theory*** Many economists have attempted to simplify the preliminary study of the distribution of income by thinking in terms of a "national goods-heap," to which each individual brings and contributes the economic goods which he has been able to produce in a given period and from which he secures the various commodities and services which he desires. In a capitalistic system, productive wealth is privately owned for the most part, and individuals are able to contribute to and receive from the goods-heap

either because their personal efforts or labors have resulted in the production of commodities and services or because they own land or capital which has been able to make a contribution to the productive process Under such a simplified concept of distribution, it is obvious to most persons that each individual should be allowed to take commodities and services out of the goods-heap in proportion to the contribution which he or some productive agent owned by him has been able to make to the goods heap He will have no desire to take out the same commodities or services which he has put in, but the commodities and services removed will be expected to have the same total value as those which were contributed

Although it is not feasible to go further with the study of distribution in these simple terms, we may note that the conclusion which has just been reached is also that of the theory of distribution which is most popular among the economists in capitalistic countries today According to this theory, the rate of remuneration received by the owners of a particular grade of a productive agent tends to be determined by demand and supply, in the long run and under competitive conditions, so that it equals the marginal productivity of the grade of the productive agent in question or the marginal contribution which this productive agent is able to make to the exchange value of commodities and services We are assuming, of course, that the units of a particular grade of a productive agent are so nearly alike that they may be interchanged in production and that they are able to contribute to the production of a number of different commodities and services with varying exchange values If only a few units of the particular grade of a productive factor are available, the rational allocation of productive resources requires that these units be reserved for their most important uses (most important, that is, from the point of view of creating exchange value and not necessarily from that of social utility or welfare) If a large number of units of the agent of production are available, they can be employed fully only if some of them are devoted to relatively unimportant uses—that is, to the production of economic goods which have comparatively little exchange value

Under any given supply conditions for the productive factor, it is the exchange value which is created by the agent in its least important use which is important in determining the rate of remuneration which will be received by the owners of all units of the agent Since these units are like and interchangeable, the loss of any

unit whatsoever would deprive us, in the long run, only of the productivity of the agent in its least important use. That is, the uses of the agent would be reorganized so that the only use lost would be the one "off the end" or the least important or marginal use. In consumption, if I consume a certain number of gallons of water in a day and I am deprived of those units which would ordinarily be used for drinking, I shall move the units which would ordinarily be used for sprinkling the lawn up to the more important drinking use and the only use of water which I shall lose will be its least important use. This same analysis is applicable to the use of productive agents and it is impossible to impute greater importance or productivity to any unit of a given grade of a productive agent than that of the marginal unit.

Now long before any unit of a productive agent would be devoted to the fifth or sixth most important use, it would be profitable to devote more than one unit of the agent to the most important use. In fact, we should use a unit of the agent for the second most important use only when it appears that the first unit devoted to this use will create more exchange value than would another unit devoted to the most important use, and so on down the line. The production of the various economic goods would be carried so far that the productivity of the last unit of the agent in the most important use would be equal to that of the last unit of the agent in any other use, and even in the last or marginal use of the agent. Thus we see that there is both an intensive and an extensive margin in the utilization of a given grade of a productive agent and that the marginal productivity of the agent will tend to be the same at both margins, in the long run under competitive conditions. These observations complicate the explanation to some extent, but they do not affect the essential conclusion, which is that all owners of units of a given grade of a productive agent tend to receive a rate of remuneration that depends upon the productivity of the agent in its marginal or least important uses, in the long run under competition. Bearing in mind possible reflex influences of rates of remuneration on supplies of the productive agents, when we apply the same analysis to all other grades of the same productive agent and to all the grades of other productive agents, we have a general theory of distribution which suggests how first the money income and then the real income of a capitalistic economy will be apportioned among the owners of various grades of the productive agents.

*The Assumptions of Distribution Theory* The general theory of income distribution is based upon a considerable number of assumptions. Specifically, the theory assumes that (1) there are many demanders and suppliers of each productive agent or grade of an agent, (2) the users of any agent compete actively for the available units of the agent, and the owners of the agent compete actively for the available opportunities for its employment, with no combinations, organizations, or conspiracies on either side of the market, (3) the owners of any productive agent and those who use it in production are reasonably well informed concerning market conditions which affect the agent, (4) each agent of production is mobile as between places and occupations, (5) there is equality of bargaining power between the suppliers and demanders of each productive agent, (6) the government does not interfere in the distributive process, and the rates of remuneration for owners of productive factors are determined exclusively by demand and supply factors in the market, and (7) the enterprises who demand the productive agents sell their own finished products under competitive market conditions.

If all these assumptions are realized in practice, the distribution of income in actual economic life will be like that envisaged by the general theory. In a work of this kind, we cannot take time to analyze each of these assumptions in detail, to decide to what extent each assumption is realized or not realized in practice, and to specify the effect of the nonrealization of each assumption on the various distributive shares. We may say, however, that these various assumptions are seldom, if ever, completely true or completely false as descriptions of actual market conditions in connection with distribution in capitalistic economies. The extent to which they are realized in practical situations varies from one time to another in regard to the same agent of production and varies from one agent of production to another at the same time. While any of the assumptions may be invalid at particular times and for particular grades of productive agents, the assumption that the government does not interfere in the distribution of income has been becoming less and less true in capitalistic economies in recent years. In the United States, for example, the federal government in the war period was interfering with or determining rents in many areas of the country, it had in effect both a law promoting and supporting organizations of workers for purposes of collective bargaining with employers and a

law specifying minimum wages and maximum hours for employees of firms operating in interstate commerce, it had been carrying on financial policies which had had a considerable effect on interest rates in the economy, and it was profoundly changing the final distribution of money income by means of heavy progressive taxes on incomes and excess profits. In general, considering the assumptions of distribution theory as a whole, it is necessary to conclude that the distribution of income specified by the general theory is only the roughest kind of an approximation of the distribution which occurs in actual practice in our economic system. In fact, some critics would go much farther and consider the general theory a complete failure as a description of reality. They would say that the distribution of income in our capitalistic system is subject to no principles or laws, save the law of the jungle. Each individual strives to get as much income as he can for himself regardless of the amount of his contribution to production. He takes who has the power, and he keeps who can.

*Functional Distribution in 1948.* According to one estimate, the total national income of the United States amounted to 224.4 billion dollars in 1948. Salary and wage payments to individuals amounted to 139.4 billion dollars, or almost 63 per cent of the total. The income of unincorporated enterprises (and adjustment in their inventory valuation) plus rental income amounted to 50.9 billion dollars, corporate profits and inventory valuation adjustment to 29.2 billion dollars, and net interest to 4.9 billion dollars.<sup>1</sup> Such broad estimates have some use in comparing economic systems but they do not tell us many things which we would like to know. For example, we do not know how the large item for wages and salaries was divided as between the wages of ordinary types of workers and the salaries going to business managers and officials. Were all the workers fairly well paid, or did most of them receive very low incomes while a few received extremely large ones? Did some of the large salaries and bonuses paid to corporate officials contain, as they often do, an element of profits? Did profits, as they often do when computed from the business point of view, contain elements of income which should have been imputed to certain other productive factors? Finally, statistics for the national income as a whole and for the broad shares of income going to the owners of productive factors

<sup>1</sup> *Survey of Current Business*, February, 1949, p. 10.

tell us nothing as to the incomes which the citizens of the economy received as individuals and as families.

*Personal or Family Distribution of Income.* While the national income is produced by the collaboration of the productive agents and is received by the owners of these agents, it is consumed in the last analysis by individuals and families, and the factor which is important in connection with their standard of living and general economic welfare is the amount of income received per individual or per family *from all sources*, rather than the rate at which income is paid for each unit of land, labor, capital, or management. The most striking fact in the personal or family distribution of income in the United States is the existence of tremendous inequality. Many millions of income receivers have low or less than-average incomes, while a relatively small number of persons and families have extremely large incomes. The highest incomes received by individuals or families are literally thousands of times as great as the incomes received by other individuals or families at the lower end of the income scale, some individuals or families receiving \$1,000,000 or more per year while others get less than \$500, or even less than \$250, per year.

In 1929, more than 21 per cent of all the families in the United States had incomes of less than \$1000, more than 42 per cent had incomes of less than \$1500, almost 60 per cent had incomes of less than \$2000, and almost 92 per cent had incomes of less than \$5000. The 8 per cent of all the families, which had incomes of \$5000 or more in 1929, controlled altogether some 42 per cent of the total income of all families. As shown in Table 16, the highest 10 per cent of the families in 1929 received 46 per cent of the total income of all families, while the lowest 10 per cent received only 1 per cent of this total income, and the lower 90 per cent received only 54 per cent. The upper half of the families in 1929 received 81 per cent of the total income of all families, while the lower half received only 19 per cent.<sup>2</sup> The income distributed by families included some 83 per cent of the total national income, the remainder being received by unattached individuals.

An investigation of the distribution of income by families in the United States in the year from July 1, 1935, to June 30, 1936,

<sup>2</sup>The income data for 1929 are adapted from M. Leven, H. G. Moulton, and C. Warburton, *America's Capacity to Consume*, Washington, The Brookings Institution, 1934, Chapter 5.

showed that almost 42 per cent of all the families had incomes of less than \$1000, almost 65 per cent had incomes of less than \$1500, about 79 per cent had incomes of less than \$2000, and more than 97 per cent had incomes of less than \$5000. The families which had incomes of \$5000 or more, or less than 3 per cent of the total, received about 21 per cent of the total income of all families. If the incomes of unattached individuals were figured in, the extent of inequality in the distribution of income would become significantly greater. In 1935-36, the highest 10 per cent of the families received 36 per cent of the total income of all families, while the lowest 10

TABLE 16

*THE DISTRIBUTION OF INCOME BY FAMILIES IN THE UNITED STATES  
IN 1929, 1935-36, AND 1946*

<i>Proportions of Families (Per Cent)</i>	<i>Proportions of Total Income Received (Per Cent)</i>		
	<i>(1929)</i>	<i>(1935-36)</i>	<i>(1946)</i>
Highest 10	46	36.0	32
Second 10	13	15.0	15
Third 10	9	11.0	11
Fourth 10	7	9.5	11
Fifth 10	6	7.0	9
Sixth 10	6	7.0	7
Seventh 10	5	5.0	6
Eighth 10	4	4.5	4
Ninth 10	3	3.0	4
Lowest 10	1	2.0	1

per cent of the families received about 2 per cent of this total income, as indicated in Table 16. The highest 20 per cent of the families received one-half (51 per cent) of the total income of all families, and the other 49 per cent of the total income was received by the other 80 per cent of the families. Again, the upper half of the families garnered some 78.5 per cent of the total income of all families in 1935-36, which meant that the lower half of the families received only some 21.5 per cent of this total income.<sup>3</sup>

In 1946, the highest 10 per cent of the families received 32 per cent of the total income of all families, while the lowest 10 per cent of the families received only 1 per cent of this total income. The highest 20 per cent of the families received as usual about half (47

<sup>3</sup> United States National Resources Committee, *Consumer Incomes in the United States, Their Distribution in 1935-36* Washington, 1938.

per cent) of the total income of all families, leaving 53 per cent of the income for the other 80 per cent of the families. Dividing the income receivers into two groups, we find that the upper half of the families had 78 per cent of the total income and the lower half only 22 per cent.<sup>4</sup> The great size of the national income in terms of dollars in 1946 meant a large increase, of course, in the proportion of all families receiving more than a fixed number of dollars like \$1000, \$1500, or \$5000 so a comparison with other years on this point would have little significance. These various studies suggest that, while the exact figures change to some extent from one year

TABLE 17

*THE DISTRIBUTION OF WEALTH IN GREAT BRITAIN  
IN 1912 AND 1924*

<i>Proportions of Wealth Owners 1912 (Per cent)</i>	<i>Proportions of Total Wealth Owned, 1912 (Per cent)</i>	<i>Proportions of Wealth Owners, 1924 (Per cent)</i>	<i>Proportions of Total Wealth Owned, 1924 (Per cent)</i>
0 2	43 2	0 04	24 9
0 5	57 5	0 1	33 4
0 9	67 0	0 3	43 0
3 3	82 9	0 8	57 0
13 3	92 9	1 6	66 7
		6 0	83 6
		23 0	93 8

to another, the general picture of income distribution by families remains relatively constant. That is, in general the upper 20 per cent of the income receivers of the United States will receive half or more of the total income of all receivers, leaving half or less of this total income for the other four-fifths of the families, and the upper half of the income receivers will receive three-fourths or more of the total income, leaving one-fourth or less for the other half of the receivers.

*The Distribution of Wealth.* Inequality in the distribution of wealth is always greater than that in the distribution of income. Individuals and families must have some income in order to live, but they are quite able to live after a fashion without owning any appreciable amount of wealth. Studies of the distribution of wealth are not often made, so we shall refer to the distribution of wealth in Great Britain in 1912 and 1924 by way of illustration.

<sup>4</sup> W. N. Peich and W. Krause, *Basic Data of the American Economy*, p. 23.

As the data in Table 17 show, well over half the wealth of the country was owned by 0.5 per cent of the wealth owners in 1912 and by 0.8 per cent of the wealth owners in 1924. Two-thirds of the total wealth was owned by 0.9 per cent of the owners in 1912 and by 1.6 per cent of the owners in 1924. Some 93 to 94 per cent of all the wealth was owned by 13.3 per cent of the owners in 1912 and by 23.0 per cent of the owners in 1924.<sup>5</sup> Conditions in the United States and other capitalistic countries were undoubtedly somewhat similar. Inequality in the distribution of wealth is closely connected with inequality in the distribution of income, since it means that the income from property will be concentrated in relatively few hands.

*The Wastefulness of Inequality* Many staunch supporters of capitalism still regard inequality in the distribution of income with respectful enthusiasm and consider it as an economic phenomenon which is not only inevitable but admirable and exhilarating. Moreover, they seem to think that anyone who dares to criticize inequality is unworthy to be a member of a capitalistic society and should be cast forth into the outer darkness. As Tawney has said,

And who does not know that to approach the question of economic equality is to enter a region haunted, not, indeed, "by hobgoblins, satyrs and dragons of the pit," yet by a host of hardly less formidable terrors—"dolesful voices and rushings to and fro," and the giant with a grim and surly voice, who shows pilgrims the skulls of those whom he has already despatched, and threatens to tear them also in pieces, and who, unlike Bunyan's giant, does not even fall into fits on sunshiny days, since in his territory the sun does not shine, and, even if it did, he would be protected against the weaknesses that beset mere theological ogies by the inflexible iron of his economic principles.<sup>6</sup>

However, with utter disregard for such fearsome warnings, we shall proceed to state some of the many criticisms which are directed at the great inequality which exists in the distribution of income in capitalistic countries.

In the first place, such inequality is said to be wasteful because it leaves large numbers of families with incomes from all sources which are too small to permit the workers to function at full efficiency. Estimates of the amount of money income necessary to maintain the family of average size on a standard of living regarded as a min-

<sup>5</sup> J. Wedgwood, *The Economics of Inheritance*. London: George Routledge and Sons, Ltd., 1929, p. 47.

<sup>6</sup> R. H. Tawney, *Inequality*. New York: Harcourt, Brace and Company, Inc., 1929, p. 29. Reprinted by permission of the publishers.

mum for "health and decency" vary considerably from one writer to another. They vary because of changes in the price level and purchasing power of money from time to time and place to place as well as because of differences of opinion between writers as to the items which simply must be included in such a minimum standard of living. However, the estimates have ranged frequently from \$1500 to \$2000 per year or even more. On the basis of the low estimate of \$1500, it would be necessary to decide that some 65 per cent, or almost two thirds, of all families in the United States failed to receive a money income in 1935-36 which would have provided them with such a minimum standard of living for health and decency. If \$2000 per year were taken as the amount of money income necessary for the minimum standard of living, 79 per cent or almost four-fifths of the families in the United States fell short of the minimum standard in 1935-36.

The results of this situation cannot be measured accurately but they are simple to describe. When family incomes are below the minimum standard for health and decency, when workers have to get along with inadequate food, clothing, and shelter, when they have to stay at their machines in spite of illness because they cannot afford to take time off, when they must go back to work because of financial considerations even though inadequately recovered from serious illness or accident, when they must get along with a program of all work and no play or recreation, it is very unlikely that the efficiency of these workers can be anything like fully maintained. When incomes are inadequate for current consumption, millions of families find it impossible to save for financial emergencies, and the efficiency of workers suffers as a result of economic insecurity. They know only too well the devastating effects which they and their families will suffer if they become unemployed because of depressed business conditions, if they are incapacitated by illness or injury, or if they lose their jobs because they become too old for industrial or business employment long before their needs and wants as consumers have ceased. It is reported that Damocles, in ancient times, was greatly upset by a single sword suspended by a hair above his head. To what extent must the efficiency of workers be reduced by this bevy of swords dangling over them as they work! Needless to say, an adequate system of social insurance of all kinds would go far toward removing the effects of economic insecurity, but few people would argue that the present system of social insurance in

the United States is so satisfactory that it relieves workers of all their worries connected with unemployment and other matters

The wastefulness of the very low incomes received by millions of American families does not end with the relative inefficiency of present-day workers. We must also consider the effects of low family income on the young members of the worker's family. When the children of the poor grow up under miserable home conditions in an atmosphere of poverty and despair, when they are unable to take full advantage of educational opportunities because they lack food and clothing, medical attention, or aids to sight and hearing, when they are compelled to leave school at an early age and get a job in order to help with the support of their families, society suffers an other loss of great but unmeasurable proportions. When the mental and physical development of workers' children is blighted by low family incomes, the potential efficiency of our economic machine suffers also.

The wastefulness of extreme inequality in the distribution of income is not limited entirely to the lower end of the income scale. Some persons with large incomes are active and industrious, but there are others who really merit the title of "idle rich" and consume heavily though they make no personal contribution to the productive process. They are, of course, willing enough to let business enterprises use, in return for a generous compensation, the land and capital which in many cases they own as a result of inheritance rather than as a result of their own efforts in the past, but they do not engage directly in productive activity. The amount of productive ability which goes to waste in this way is probably not extremely large in the aggregate, but most of these persons could probably produce something, if it were impossible for them to lead a life of luxury without working.

*The Misguidance of Production.* Inequality in the distribution of income is wasteful in that it results, from the social point of view, in the misguidance or misdirection of production. This result occurs because great inequality sharply reduces the accuracy with which the prices of various goods on the market measure the relative intensities of human desires for these goods. As we have seen in an earlier chapter, the production of economic goods under capitalism is supposed to become adjusted to the needs and desires of consumers through the price mechanism. If consumers were rational and had equal incomes, they would be willing to pay highest prices

for economic goods that they valued most and lowest prices for goods that they valued least. On the other hand, business enterprises under the influence of economic motivation would be attracted to the lines of production whose products commanded high prices in relation to their costs and would leave or fail to enter lines of production whose products sold for prices which were low in relation to their costs. In somewhat similar fashion, other productive agents would be drawn into the favorable lines of production and out of the unfavorable lines. Thus, as a result, the goods that were most strongly desired would be produced in largest quantities, those that were least desired would be produced in smallest amounts, and market equilibrium on the basis of prices would come much closer than it actually does to being an economic optimum.

Under conditions of extreme inequality in the distribution of income, persons with very large incomes may be willing to pay relatively high prices for commodities and services which are unimportant to them and which furnish only a trivial amount of satisfaction, while individuals with very low incomes may be able to pay only very low prices for the commodities and services which are vital to their health and welfare. In this situation, enterprises in following the profit motive are likely to produce luxuries and trivialities for the rich while the poor go without the necessities of life, for enterprisers cannot bother to investigate the reasons why some prices are high and profitable while others are low and unprofitable, if indeed they are even interested in knowing. While people with small incomes cannot obtain adequate quantities of badly needed commodities and services, rich people can command 3 million dollar mansions, 5 million dollar yachts, 51 cars to the family, million dollar coming-out parties, hose at \$2000 per pair, perfume at \$1800 per ounce, and mink coats and air-conditioned dog houses for their pets. Now it may seem to the rich that there is no misguidance of production in this situation, and the same impression may be held by those who find extreme inequality in the distribution of income not only inevitable but admirable and exhilarating. However, the misguidance may be seen by comparing a capitalistic society with one in which production would be based on social need, for such a society would surely produce necessities for all before needless luxuries were produced for anyone.

*The Utility of the National Income.* Another closely related criticism which turns on the question of utility suggests that great in-

equality in the distribution of income prevents us from obtaining the maximum possible aggregate of satisfactions from the consumption of the national income. If we assume rationality of behavior, an individual should spend his first, say, \$500 of money income in a given period for those economic goods which he needs or desires most. A second increment of \$500 would also be spent for important goods, but these goods would not be so vitally necessary as those secured with the first installment of income, and so on, until the \$500 which made a person's income \$1,000,000 instead of \$999,500 would be very unimportant indeed. Like the persons on the Lord High Executioner's list in *The Mikado*, it never would be missed. Even the receipt of money income may be subject to the Law of Diminishing Utility. If \$500 or some other sum were taken from a person with a very large annual income, it would reduce his aggregate satisfactions almost infinitesimally, while the same sum added to the income of a person who now receives only \$1000 or \$1500 per year would increase his aggregate satisfactions greatly. Thus, the conclusion is that the aggregate satisfactions derived from the consumption of the national income would be greatly increased if this income were more equally divided on a personal or family basis than at present.

Both of these arguments concerning utility rest on somewhat unsatisfactory grounds. That is, they involve inter-personal comparisons of utilities or satisfactions, and there is no way in which such comparisons can be made effectively. Since utility or satisfaction is a subjective affair, we cannot *prove* that the rich people enjoy their luxuries less than the poor people enjoy their necessities or that one man enjoys his tenth \$500 increment of money income less than another enjoys his fifth \$500 increment. In fact, it is frequently contended that some people have greater capacity for experiencing satisfactions or gratifications than others. If this is true (and it is not susceptible to proof), an equal division of income would be undesirable from the point of view of maximizing the aggregate satisfactions derived from the national income. However, it seems very doubtful that some persons have capacities for experiencing satisfactions which are thousands of times as great as those of other persons, and differences in income of this magnitude between persons are probably not justified from the point of view of deriving maximum aggregate satisfaction from the national income.

*Inequality and the Business Cycle* Inequality in the distribution of income is the basis of the famous and popular underconsumption theory of the business cycle. According to this theory, some persons have such large money incomes that they cannot spend them all in consumption. They save large quantities of funds and usually invest them directly or indirectly in new productive facilities. But these additional productive facilities are useless or worse than useless unless the goods which they eventually will place on the market can find purchasers. Moreover, the great masses of consumers who must buy these products, if they are to be sold, have such small money incomes that they cannot purchase the goods which are produced for them. When large quantities of unsold goods pile up on the markets of the country, productive facilities can no longer be operated profitably, and a depression occurs.

The underconsumption theory of the business cycle, in this very simple form, has few supporters among economists today. In the first place, there is quite a logical gap in the behavior which it attributes to persons of large income, for it assumes that they invest blindly in new productive facilities without much thought of a return on their investments and then cease to operate their productive facilities as soon as they fail to produce a return. Again, it is not entirely certain that more saving and capital formation will occur in an economy in which great inequality prevails in the distribution of income than in one in which income is more equally divided. Soviet Russia has had much less inequality in the division of income than most capitalistic countries and yet she has carried on saving and capital formation at a tremendous rate. Moreover, the existence of a great volume of saving and investment has not prevented the Russian consumers from taking off the market all the consumers' goods and services which could be made available for them.

Even if more saving and capital formation should occur where great inequality is present, no baffling problem is necessarily created. On the basis of the market and price mechanism, it should be possible to arrange the system of production so that it will turn out a national income composed of 80 per cent consumers' goods and 20 per cent capital goods just as easily as it could produce 90 per cent consumers' goods and 10 per cent capital goods. To be sure, if 20 per cent capital goods are produced instead of 10 per cent, the volume of production of consumers' goods in the future will be increased more rapidly and trouble will be encountered unless these

additional goods can be sold. But there should be no difficulty in selling the goods if their prices are flexible and decline as additional goods are produced at lower costs. If an attempt is made to sell larger and larger amounts of consumers' goods at stable or rising prices to great numbers of consumers whose incomes do not increase significantly, underconsumption and depression may result, but many conditions besides mere inequality in the distribution of income are involved in this result.

There is one way in which inequality in the distribution of income may be closely connected with the events of the business cycle. Since wages ordinarily go up more slowly than the price level in general, while profits and other types of income which go to make up the larger incomes of individuals increase rapidly in periods of prosperity, it may be that in major boom periods inequality in the distribution of income will increase significantly. If this occurs and the recipients of the large increasing incomes save unusually large proportions of these incomes, the income receivers of the economy as a whole may be calling for a relationship of 75 to 25 as between consumers' goods and capital goods at the end of a boom period, whereas the productive facilities of the economy are geared to an 85 to 15 relationship, and misdirected production and underconsumption may apparently occur. For example, in 1922, wages and salaries were 55.06 per cent of total income in the United States, dividends were 10.71 per cent, and other property incomes 34.23 per cent. In 1929, wages and salaries were 37.40 per cent of total income, dividends 15.98 per cent, and other property incomes 46.62 per cent. Over the whole period, while the national income increased about a third, the total incomes of persons receiving \$50,000 or more per year increased 241 per cent, those of persons receiving from \$10,000 to \$50,000 increased 79 per cent, those of persons receiving from \$5000 to \$10,000 increased 67 per cent, and those of persons receiving less than \$5000 actually declined.<sup>7</sup> Changes of these kinds undoubtedly play an important part in the business cycle.

*Other Results of Inequality* Finally, inequality in the distribution of income is criticized because it is said to lead to inequality in other matters. It may not be strictly correct to say that there is one law for the rich and another for the poor, but all too often the fate of

<sup>7</sup> A. B. Adams, *National Economic Security* (Norman (Okla.) University of Oklahoma Press, 1936, pp. 39 and 276-277).

an individual in either civil or criminal cases depends to a considerable extent on his wealth and income status. Inequality before the law finds its counterpart in political inequality. In theory, a capitalistic country may have political equality, but in practice a rich man may be able to control many votes besides his own, influence public opinion in favor of legislation which he desires or against that which he dislikes, control legislators directly or by lobbying, and so on. Finally, inequality in the distribution of income leads to inequality in education and culture, in social status, in business opportunities, and in many other matters.

*In Defense of Inequality* Supporters of the capitalistic system and all its works do not hesitate to defend inequality in the distribution of income. Sometimes it is said that such inequality is natural, since individuals are unequal in many other respects. This argument deserves very little consideration. Human progress throughout recorded history has depended very largely on the changing or overcoming of factors that were natural, and the fact that people are unequal in other respects is no real argument for economic inequality. As Tawney says,

Everyone sees, for example, that it is not a valid argument against women's suffrage to urge, as used to be urged not so long ago, that women are physically weaker than men, since physical strength is not relevant to the question of the ability to exercise the franchise, or a valid argument in favor of slavery that some men are less intelligent than others, since it is not certain that slavery is the most suitable penalty for lack of intelligence.<sup>8</sup>

Many people also argue that inequality in the distribution of income is inevitable, whether or not it is undesirable, and too often this argument is based simply upon the fact that several studies of income distribution in various capitalistic countries at different times have revealed not only inequality but a surprisingly consistent degree of inequality. It should be obvious, however, that inequality is not necessary in all times and under all conditions merely because it tends to prevail under certain circumstances and institutions. The argument that inequality is inevitable, though it is sometimes an effective argument, is classed by Tawney as economic Mumbo-Jumbo.

<sup>8</sup> R. H. Tawney, *Equality*, p. 40. Reprinted by permission of Harcourt, Brace and Company, Inc., New York.

But the power of Mumbo-Jumbo, like that of some other spirits, depends on the presence of an initial will to believe in the minds of his votaries, and can, if only they are not terrified when he sends forth his thunders and his lightnings—the hail of his logarithms and the whirlwind of his economic laws—be overcome If, when he tells them that a certain course will result in the heavens falling, they summon up the resolution to pursue it all the same, they will find that, in a surprising number of cases, though they may have succeeded in improving the earth, the heavens, nevertheless, remain much where they were<sup>9</sup>

*Inequality and Capital Formation* Inequality in income distribution is sometimes considered necessary to the development of an efficient and progressive economic system Efficient production must be roundabout, large-scale, and specialized, but such production requires large amounts of capital Capital formation and accumulation depend upon saving, and saving under capitalism is accomplished by individuals who have surplus incomes above their needs for current consumption If our national money income were divided equally among individuals or families, little if any saving would occur With some persons poor and others rich, we may expect individuals with large incomes to save extensively and devote the saved funds to capital purposes In this way, the rich are public benefactors

We may admit that individuals with large incomes are responsible for a considerable part of the saving and capital formation that exists in our capitalistic system It may also be true that, if the national income under capitalism were so small that, when equally divided, it furnished each individual or family with an amount of money income no greater than was needed for current consumption, saving and capital formation might languish if individuals were left to their own devices On the other hand, if the national income were great enough so that, when divided with substantial equality, it furnished immediate consumption needs, it is probable that an adequate amount of saving and capital formation would occur If it did not occur naturally, the government could step in and require additional saving and capital formation even under an essentially capitalistic system Certainly the argument concerning inequality and capital formation has little relevance for other than capitalistic systems, since it is obvious that relative equality of incomes in Russia has not stood in the way of extensive saving and capital for-

<sup>9</sup> *Ibid.*, pp. 46-47 Reprinted by permission of Harcourt, Brace and Company, Inc., New York

mation In any case, many economists today believe that the idea that nothing should ever be done which might have the effect of checking or limiting the supply of savings is simply fetishism

*Inequality and Culture* An even weaker argument holds that inequality in the distribution of income and even exploitation must be condoned, if not approved, as making for higher culture and civilization Some people must be poor and miserable in order that other persons may have surplus incomes, part of which may be devoted to the support of art, literature, and music, to the setting up of foundations for medical or educational research, and to other projects These advantages might be lost to society, it is said, if the national income were equally or almost equally divided among individuals or families But many people would contend that these various projects should not be carried on so long as the national income is too small to care for the current consumption needs of all the people On the other hand, if the national income were large enough so that, when rather equally divided, it gave each individual or family more than enough money income for immediate consumption needs, these would be nothing to keep these cultural and research projects from being carried on either by private subscription or by governmental action

*Inequality and Economic Incentives* Inequality in income distribution is regarded by some as a source of incentives for the individuals in our economic system If the national income were divided equally, it is asked, how would we stimulate workers to produce efficiently? How would we get the individual to accept the most difficult and responsible position in economic life for which he can qualify? How would we get people to be business enterprisers and managers if they received no more income than ordinary workers? In answer to these questions, it is said that most people will not work, or at least will not work hard, without the prospect of economic gain All trades and lines of production which are tolerated by society should be characterized by "equality of opportunity," and then all persons should be rewarded according to the results which they produce in terms of service, and not on the basis of efforts, needs, or anything else And the measure of service is what the market is willing to pay The result may be extreme inequality, but such inequality is perfectly just and necessary If our economic system is to be efficient and progressive, it is necessary to provide unusual economic rewards for unusual accomplishments

So far as we know, there is no complete and final answer to this line of argument. If our earlier analysis has been correct, the desire for economic gain is the most common and strongest motivating force at work in a capitalistic system. Considering the broad range of economic activity as a whole, no other way of getting things done is likely to be nearly so effective as appealing to the desire of individuals for pecuniary gain and economic advancement. However, even if this much is admitted, we cannot be entirely sure why it is true. Should we regard individuals as naturally acquisitive and the capitalistic system, which stresses acquisitiveness, as merely a natural outgrowth or development on the basis of the nature of individuals in the mass, or does the individual behave acquisitively under capitalism merely because he lives in a system which stresses acquisitiveness and in which behaving in that fashion is the prescribed way to get almost all the things which are regarded as worth striving for? Many supporters of capitalism clearly take the former point of view. Acquisitiveness is a part of human nature in all times and places. Unless large economic rewards are provided for unusual accomplishments, individuals will lack incentives under capitalism, and any economic system which attempts to replace economic motivation with other motivating forces is doomed to failure from the outset. Other people regard acquisitiveness distinctly as an acquired human trait, which is dependent on the existence of the peculiar institutional and environmental forces of capitalism. Whether or not great differences in rewards are necessary under capitalism, it would not be very difficult to substitute other motivating forces for acquisitiveness in some other type of economic system, according to this point of view.

We also know that individuals even under capitalism are not motivated solely by the desire to acquire large quantities of economic goods for themselves or their families. Many people apparently put forth their best efforts and accomplish excellent results in governmental or other positions whose nature is such that they can never hope for really large material rewards. Others work hard because of a desire for honors, prestige, and public acclaim, or because of habit, pride in their work, or just the fun of playing the game. Beyond certain levels of income, individuals undoubtedly work largely to obtain increased power rather than any enjoyments in consumption which additional money income may bring. In the case of millions of ordinary workers, who have no real chance to ob-

tain large earnings no matter how hard they work, the chief incentive is probably negative. That is, they fear that they will be denied access to the material means of production unless they work with reasonable diligence. Finally, in the case of the many people who are usually unemployed under capitalism, we may question whether the system furnishes any incentives at all.

Even if considerable differences in incomes are necessary under capitalism in order to furnish individuals with incentives to achievement, we have no way of knowing whether our present differentials in income are necessary for this purpose or whether they measure at all accurately the differences in productivity that exist. On the whole, it seems doubtful that the tremendous differentials in income which prevail in our system are necessary to induce our most talented individuals to make full use of their abilities. If no worker received less than \$2000 per year and incomes were carefully graduated from that level up to, say, \$25,000 per year, it might be that such differentials would be as adequate to furnish incentives to productivity for all individuals as are the much larger differentials which we actually have. Finally, we may question whether some individuals are actually thousands of times more productive than others, as the differentials in income which prevail seem to suggest. *Inequality and the Price System.* Why, then, do extremely large differentials in income exist in our capitalistic system? The primary basis for unequal incomes among individuals and families is found in income derived from the sale of labor services. The labor supply is divided up into non-competing groups in such a way that many persons can perform the functions required by occupations in the lower groups, while comparatively few persons can fill the requirements of the occupations in the higher groups. Rather large differences in the marginal productivity of units of labor service therefore exist between the labor groups, and, although wages do not adjust themselves with perfect accuracy to these inter-group differences in marginal productivity, great differences in wages or payments for labor service are found between workers in different groups. Thus, even if there were no other sources of income for the various individuals, a considerable degree of inequality in income distribution would result from this factor alone.

Actually, since our system permits private individuals to own land and capital and to turn these objects of wealth over to various enterprises on the basis of the income to be derived from their use in

production, individuals receive income for the use of their land and capital as well as for the use of their labor services. This fact might make for equality rather than inequality in the distribution of income if those individuals who had small labor incomes derived large incomes from owning land and capital while the individuals who had large incomes from the sale of labor services received little if any income from the ownership of land and capital. However, the actual situation is just the other way around. The ownership of large quantities of land and capital is usually a great help to an individual in acquiring a large labor income if he wishes to do so, while the receipt of a large labor income makes possible the acquisition of additional land and capital. Inequality in the distribution of income would be great enough in all conscience if individuals were limited to receiving income from the sale of their labor services and from the wealth which they could accumulate in their own lifetimes, but it becomes still greater when the institution of inheritance is allowed to operate. Individuals who pile up great fortunes are allowed to transfer them to their heirs, who may continue to receive income from the inherited wealth in addition to that which they derive from the sale of labor services and from wealth which they can themselves accumulate.

Fundamentally, then, inequality in income distribution is derived from the operation of the institutions of capitalism, such as private property (including inheritance), free enterprise, competition, and the pricing process. High prices are set on scarce agents of production and low prices on relatively plentiful agents—results which are desirable in many respects. High prices for the scarce agents tend to reserve these agents for the uses which are deemed most important on a price basis and keep them from being wasted in relatively unimportant uses. Low prices for the more plentiful agents tend to lead to their use in large quantities and to prevent their being wasted in unemployment as they would be if high prices were set upon them. High prices for the scarce agents tend to bring about an increase in their quantity, where such a result is possible, while low prices for the more plentiful agents tend to lead to a restriction of their quantity. Thus we see that high and low prices for various grades of productive agents not only result from the operation of the pricing system but are necessary to the rational allocation of productive resources under capitalism and to the attainment of equilibrium on the basis of market forces. On the other hand, high

prices for the relatively scarce agents mean large incomes for the owners of these agents, while low prices for the relatively plentiful agents give low incomes to the owners of these agents, and inequality in the distribution of income results.

*Remedies for Inequality* It seems to follow that, if we want a capitalistic system to operate successfully, we must look askance at schemes for reducing inequality in the distribution of income by placing arbitrary and artificial prices on the services of productive agents. If a high-powered industrial manager is worth \$100,000 a year according to the market, the existence of such a price for his services tends to reserve them for use by that firm which can derive the greatest value (product value, not necessarily social value) from them. To set an artificial price of \$10,000 a year on such a man would make it possible for any number of firms to claim him and would leave no logical method, at least in an unplanned economy, of deciding which firm should get him. A similar problem of allocation would arise, of course, if we set a rental of \$5000 per year on an urban corner lot which would readily bring \$50,000 per year in a free market.

On the other hand, to set an arbitrary minimum wage of \$2500 a year on the services of a man who never has earned and never will earn more than \$1500 a year in a free market would be to insure that he and thousands of others like him would languish in unemployment outside of a fully planned and controlled economy. Besides these problems having to do with the allocation and use of resources, there would probably be a severe problem of incentives, if we followed the policy of not letting people make widely differentiated incomes in an erstwhile capitalistic system. To set a \$10,000 salary on the business manager whose services would be worth \$100,000 a year in a free market might well induce him to do only \$10,000 worth of work annually. Such decisions, if reached by considerable numbers of people, would have most unfortunate implications for the productivity of the economy and the size of the national income which it would have to divide.

In view of these difficulties, most people who would like to do something about reducing inequality in the distribution of income while retaining the capitalistic system turn to the philosophy of "let them make it and then take it away from them" rather than that of "don't let them make it in the first place." Once individuals have received their high and low incomes on the

basis of the pricing process, heavy and progressive income taxes can be used to reduce the distance between the extremes of income. The influence of inheritance in increasing and perpetuating inequality can be reduced or largely eliminated by heavy progressive inheritance taxation. The government can use a portion of public revenues to subsidize the production of various goods for the use of the poor. It can also provide a variety of social services to improve the physical and mental development of the young. These developments might include health and medical services, medical research, infant care, maternity benefits, adequate educational facilities of all types, physical culture, and the provision of museums, theaters, and concert halls. In these ways we could hope to break down the purely environmental barriers to movement between the labor groups and permit each person to obtain the highest and most remunerative employment for which his native abilities enabled him to qualify.

In spite of these possibilities, socialists contend that nothing really significant is likely to be done about inequality under capitalism and that it is necessary to shift to a socialized society in order to obtain a real solution for the problem. There is an element of truth in this contention, for once again we have to worry about the problem of incentives if we carry the progressive taxation of incomes and inheritances too far. People may not strive to increase their incomes or to secure large incomes in the first place if our progressive taxes leave them with too little to keep for themselves. Progressive taxes may not affect incentives so severely as would a governmental policy of limiting the incomes which people may receive in the first place. If you have large quantities of income passing through your hands, there is always the chance that the government may relent and allow you to keep some of it for yourself. Moreover, there may be a certain prestige value in making a large income even if you do not get to keep it. Nevertheless, the need for adequate incentives definitely places a road-block in the way of using progressive taxes to reduce inequality greatly while trying to retain the capitalistic system.

#### QUESTIONS

- 1 On what assumptions is the general theory of income distribution under capitalism based?
- 2 "The distribution of income specified by economic theory is only the

- roughest kind of an approximation of the distribution which occurs in actual practice in our economic system" Show whether you agree
- 3 "The most striking feature of the personal distribution of income in the United States is its extreme inequality" Discuss
- 4 "Statistics on the distribution of income by families in the United States for 1929, 1935 36, and 1946 suggest that inequality is decreasing gradually" Show whether you agree
- 5 "Inequality in the distribution of ownership of wealth under capitalism is always much greater than that in the distribution of income" Explain
- 6 "Extreme inequality in the distribution of income decreases the efficiency of production" Do you agree? Explain
- 7 Why is it argued that great inequality in the distribution of income results in the misguidance of production? Explain
- 8 How does inequality in income distribution prevent the realization of the greatest possible aggregate of satisfactions from the consumption of the national income? Explain
- 9 Discuss the significance of great inequality in the distribution of income in relation to business cycles under capitalism
- 10 "Inequality in the distribution of income leads to inequality between persons with respect to other matters" Do you agree? Explain
- 11 "Considerable inequality in the distribution of income is necessary in order that there may be adequate saving and capital formation under capitalism" Show whether you agree
- 12 "If our economic system is to be efficient and progressive, it is necessary to provide unusual economic rewards for the unusual accomplishments of individuals Hence, great inequality in the distribution of income is necessary and desirable" Show whether you agree
- 13 "Great inequality in the distribution of income is necessary in order that adequate incentives to efficiency and productivity may exist in our capitalistic economic system" Do you agree? Explain
- 14 Why does great inequality in the distribution of income exist in our capitalistic system? Explain
- 15 "Though the result is inequality in the distribution of income, it is economically desirable that high prices be set on the relatively scarce productive agents and low prices on the more plentiful agents" Explain
- 16 What can be done under capitalism to reduce inequality in the distribution of income or to mitigate some of its unfortunate effects? Explain
- 17 If you felt that inequality in the distribution of income must be reduced under capitalism, would you try to keep people from making highly unequal incomes in the first place, or let them make such incomes and then reduce inequality through taxation? Why?

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## CHAPTER 16

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### THE DISTRIBUTION OF INCOME

(Continued)

#### *The Distribution of Income under Socialism and Communism*

***The Elimination of Property Incomes*** Under socialism, the people as a whole, operating through the government, would own virtually all productive wealth and operate practically all important economic enterprises There would be no landowners as a separate group receiving rent as a share of the national income Whether there would be any interest would depend on the way in which the socialistic society operated If the government paid out to the people more than enough money income to buy all the available consumers' goods and services and then sought to recapture a part of this money income for capital purposes by means of various devices which we have already examined, interest might exist in a small way as a separate share in distribution That is, interest would probably be paid on deposits which the people made in savings banks operated by the government and on government bonds purchased by the citizens However, individuals could not directly own any important quantities of capital goods, and interest payments, if they existed, would be relatively insignificant Profits would also be virtually eliminated as a private share in distribution because of the public operation of most enterprises

All this is what the socialists mean when they say that rent, interest, and profits would be eliminated in their system They do not and cannot mean that the factors or forces which give rise to rent, interest, and profits under capitalism could all be eliminated under socialism Land would still be of various grades and qualities under socialism, and a given amount of labor and capital applied

to high grade land would still be more productive than if it were used on low-grade land. The differential surplus, instead of resulting in rent for individual owners of high-grade land, would merely belong to society as a whole. It could be paid out to all the workers as a part of their wages, or the government could retain it for purposes of capital development or the rendering of various social services. In similar fashion, under socialism as under capitalism, production by means of the roundabout process using large amounts of capital would be more efficient than direct production, and saving would be necessary in order that capital formation might take place. The saving process would still be costly inasmuch as individuals would undoubtedly continue to prefer present goods to future goods, other things equal, even under socialism. However, the burden of saving would fall, in general, on all members of society under socialism and would be effected by their going without consumers' goods in the present. The increased quantities of economic goods which roundabout production would make available in the future would then be shared by all members of society in the form of increased real wages, or in other ways.

Finally, the conditions which give rise to profits could hardly be completely eliminated under socialism. While some risks might be removed or reduced, weather and other natural conditions would still remain uncontrollable, and the actual efficiency of workers might be much greater or less than had been planned. However, any failures of production to come up to expectations, or any successes in getting production to exceed planned estimates would be of concern to the members of society as a whole and not to a particular class of private enterprisers. It should be obvious that the distribution of income under socialism would be quite different from that which prevails under capitalism and that our usual theories of distribution would be worthless in connection with a socialistic economy. Descriptions of the determination of rent and interest in terms of marginal productivity and other factors are not very helpful in the study of an economic system in which individuals are not allowed to receive these returns as private income or own the agents which produce the returns.

*Wages under Socialism.* Practically all income available for consumption would be received first as money wages and later as real wages under socialism, but there is some question as to what wages would be like. Some socialists contend that equal wages should be

paid to all under socialism in the interests of fairness and justice. But what is meant by equal wages? If equal wages were paid to each worker actually employed, families with several breadwinners would be more adequately provided for than those with only one. If equal incomes were paid to all individuals regardless of age, the large families would in general be in better circumstances than the small families, since the very young and the very old may not consume nearly so much as other members of the family and since there are certain obvious economies involved in consuming in large family groups. A family of ten will not require five times as much gas for cooking as a family of two, five times as much electricity for lighting, nor five times as much fuel for heating, and its food bill should not be five times as large. Moreover, such an emphasis on the desirability of large families might cause the Malthusian bogey of overpopulation to raise its ugly head again.

If equal incomes were paid on a family basis, the small families would have a distinct edge over the large ones, and the danger of having too small a population might replace that of overpopulation. Apparently, equality is a very difficult objective to attain, even given the best of intentions. If substantial equality of income were the goal, perhaps the best system would be one of roughly equal wages for adults, with smaller allowances for dependent children and other dependents, and perhaps special allowances for mothers or individuals in particular occupations. Even if some way could be found to achieve substantial equality in the distribution of money income, we should still not be out of the woods, for individuals differ considerably in the matter of their needs and desires, and equal money incomes would treat them rather unequally on this basis. Of course, the socialists might try to "educate" people so that they would want very much the same things. Finally, equality with respect to money income would leave some individuals or families very much better off than others because, as we see under capitalism, some individuals and families are much better able to manage income than others and get much more out of a given amount of money income. Something could be done about this problem through education too, but it is clear that the general problem of achieving equality is a rather difficult one.

On the whole, it is unlikely that a socialistic economy would attempt to achieve equal incomes. The planners would have enough difficulties in making decisions relative to cost with the prices of

costs of land and capital arbitrarily determined, and it would be desirable, if possible, to have labor costs real instead of artificial. Moreover, we must remember that wages are not to be regarded solely as a reward for productive accomplishments. They are also a means of allocating labor among occupations and industries. Under equal wages and in the absence of governmental compulsion, labor would probably pile up in certain occupations and industries while shortages of labor would exist elsewhere. Land and capital could be arbitrarily assigned to different lines of production by the economic planners, but it would be neither humane nor economically wise to accord workers the same treatment. Thus, wage differentials between industries and occupations would probably be set up for the purpose of inducing workers to distribute themselves among occupations and industries in a manner deemed appropriate to the carrying out of the economic plans of the system.

Thus, the general prospectus for socialism holds that people should work according to their desire for compensation and receive income in accordance with the quantity and quality of work done. In other words, wages would presumably be paid on the basis of productivity, but we should not jump to the conclusion that differentials in wages under socialism would be comparable to those which exist under capitalism. In the first place, the workers' productivity and wages would depend on social value rather than exchange value. Some occupations which are open to workers under capitalism would not be available at all under socialism. Moreover, the value of all final products of labor, and hence indirectly the value imputable to labor itself, would be determined by economic planning on the basis of social need and not by the free operation of the market. It is doubtful if such planning on the basis of social need would set up differentials in the evaluation of labor services which were anything like as large as those which result from the market determination of exchange values under capitalism. Again differentials in wages would be smaller under socialism than under capitalism, even on a productivity basis, because workers would not differ as greatly in productive ability as they do under capitalism. Socialism aims to give every individual as much education and training as he can absorb, and in general to break down all environmental barriers to movements between the labor groups. With more workers able to qualify for positions in the higher labor groups and fewer workers compelled to remain behind in the lower groups,

differences in marginal productivity between the groups would be minimized and so would the necessary differences in wages.

*Inequality under Socialism* Nevertheless, there would still be differences in wages under socialism and inequality would exist in the distribution of income. We should like very much to know just how great this inequality would be, but this is something which it is difficult to predict accurately in advance, since it would depend not only on the relative productivity of the different workers but also on the need to establish wage differentials which would result in an appropriate distribution of workers among occupations and industries. Some socialists suggest tentatively that differentials in wages from top to bottom might be something on the order of 15 to 1. If differences in wages could be held down to anything like this ratio, inequality in the distribution of income under socialism would be extremely slight in comparison with that of capitalistic countries. The government under socialism would also furnish a large volume of social services, and, if these services were distributed equally among the workers receiving high and low wages or were given in greater volume to workers (and their families) receiving low wages than to workers receiving high wages, inequality in the distribution of real income would be less than that in the distribution of money income.

The inequality in the distribution of money income which existed under socialism could not accomplish any important ill effects in any case. The receivers of large incomes could enjoy a somewhat higher standard of living than the receivers of small incomes, but that is about all. They could not use their large incomes to acquire land and capital nor could they pile up large fortunes for their heirs and dependents. They could not use their large incomes to direct productive agents into the production of yachts, limousines, elaborate mansions, and other expensive luxuries, because decisions as to the kinds and quantities of economic goods to be produced would be made ultimately by the economic planners and not by private, profit-seeking enterprisers. In spite of inequality in incomes, necessities for all would come before luxuries for any. The receivers of large incomes could not indulge in over-saving, for decisions as to saving and capital formation would also be made by the economic planners, and no volume of saving decided upon would be so great as to make it impossible for the consumers of the system to take the available commodities and services off the market. Neither would it

be very difficult to justify the existence of moderate inequality in income distribution under socialism, for the goal of socialism is the abolition of social classes rather than the achievement of perfect equality of incomes. It is the source of the individual's income, rather than the amount of it, which is decisive.

*Incentives under Socialism* Would the small differences in incomes which modern socialism contemplates prove adequate to provide incentives for all? The socialists obviously think that they would, but this is another matter which can be fully determined only by experience. The socialists contend that an individual would not mind being only fairly prosperous if there were no very rich individuals with whom he could compare himself unfavorably. The socialists do not expect that individuals who are accustomed to receiving large incomes under capitalism will ever be fully content with the smaller rewards available under socialism. But they expect that, as soon as a new generation comes along which is composed of individuals who know nothing of the large differentials in income which used to prevail under capitalism, people will work just as hard and efficiently under the small income differentials of socialism as they would under any other system of rewards. This argument would be fairly convincing if it did not remind one so much of the argument which was once used in connection with prohibition in the United States. Supporters of prohibition contended that they did not expect to reform individuals who were already confirmed drunkards and insisted that prohibition would really begin to work effectively when a new generation had grown up whose members had never seen a saloon. As everyone remembers, the expectations of these people were much less than completely realized.

In any case, the socialists do not intend to rely entirely on differences in wages to provide incentives for the people. They intend to reduce the importance of economic motivation as much as possible while developing other types of incentives greatly. Individuals under socialism would work for power, prestige, public honors, and acclaim. Exceptionally valiant workers could be admitted to honorary orders or societies, busts and statues could be set up in their honor, they could be given medals, and their names and accomplishments could be respectfully mentioned over the radio and in the newspapers. They would take pride in their work, know the joys of creation, and have the fun of playing the game. They would be influenced by the opportunity for education and training, by having

work suited to their individual abilities, by the certainty of having a job, by complete relief from social insecurity, by knowing that the more responsible positions would be filled on the basis of merit, by the prospect of more pleasant and interesting work in advanced positions, by the knowledge that, under fairly equal incomes, they could benefit themselves by working to increase the social product, and by idealism, altruism, and devotion to the cause. They would also be subject to ultimate compulsion, since they would have to work to obtain a living. However, this requirement would apply to all, and everyone would have a chance to make a living. Under social pressure, idleness would be a ground for social reproach and a fair day's work would be a social obligation. The slacker would be aware of despoiling his fellows as well as himself. Penalties could be provided for unsatisfactory work and other shortcomings on the part of the workers.

Many confirmed supporters of capitalism are very dubious about the success with which a socialistic economy could depend upon the so-called non-economic types of incentives. But, as Cole says, "It is hardly surprising if, under a [capitalistic] system which threatens men with ruin unless they keep their eyes steadily on the main chance, the majority of people are actually impelled to work largely by selfish material motives." But evidence of how men behave when they are subjected to the stimulus of one set of motives is by no means sufficient evidence of their probable behavior under the influence of quite different stimuli.<sup>1</sup> Some incentives other than those which involve differential incomes operate fairly well even under capitalism, and, if they were removed from the dark shadow of acquisitiveness under socialism, they might well become even more effective. In any case, even if incentives proved inadequate under socialism, the socialists contend that an economy would be better off with a moderate-sized national income distributed on a basis of substantial equality than with a larger national income most of which went to relatively small number of receivers of large incomes. And in this argument, it seems, the socialists may really have something.

*The Distribution of Income under Communism.* The distribution of income under ideal communism would be exceedingly simple. There would be no money income to distribute nor would there be

<sup>1</sup> G. D. H. Cole, *The Simple Case for Socialism*, p. 53. Reprinted by permission of Victor Gollancz, Ltd., London.

any shares in distribution as such. Each able person would be expected to work according to his ability, and to receive real income according to his needs, without reference to productivity. Differences in income would exist only to the extent that there were differences in needs from one individual to another. Economic incentives involving differential incomes would be abandoned and complete reliance would be placed on other types of incentives. Many economists would believe that an economic system could operate effectively on this basis only when they actually saw it happen. At the very best, communism could be achieved only after many decades if not centuries of socialism.

### *The Distribution of Income in Soviet Russia*

*Property Incomes* In matters of income distribution, Soviet Russia measures up to the specifications of theoretical or ideal socialism fairly well. The land of the country is owned by the state in the name of the people and there is no separate class of people who, as landowners, receive rent as private income. The collective farmers have been given the right to use their land in perpetuity, and this is almost the same as ownership, but the special taxes which these farmers must pay to the government are said to be enough or more than enough to cover the rents which, under other circumstances, the collective farmers might have had to pay to private landowners. Practically all the capital of the country is owned either by the state or by state-approved cooperative associations, but interest does figure in the national income to some extent. A part of the income received by private peasants, artisans, and other individual producers may be construed as interest on the relatively small amounts of capital which they own, and the same thing is true of part of the income received by the collective farmers and members of other types of producers' cooperatives.

In 1940, when the national budget expenditures amounted to 173.3 billion rubles altogether, interest on the public debt called for expenditures of 2.8 billion rubles, or 1.6 per cent of the total.<sup>2</sup> The public debt increased considerably during World War II, but interest rates remained low and total interest payments on the debt are still a very insignificant part of the national income. A part of the interest on the debt goes to private individuals as bond owners,

<sup>2</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 137.

while the rest goes to savings banks and other institutions with investments in government bonds. Interest is also paid on the deposits of individuals in the savings banks of the country. At the end of World War II, these deposits had regained the prewar level of about 73 billion rubles, but the interest on them could not have amounted to much over 200 million rubles.

The governmental enterprises in various fields of economic activity make both planned and unplanned profits at times, but the significance of these profits is quite different from that of profits in a capitalistic country. They belong to the government and are used for capital development, social services, and other purposes. Under capitalism, a relatively small part of the people own the industries and receive the profits, but in Russia all the people own the industries and receive the benefit of profits when they are made. Opportunities for profit on the part of private and cooperative enterprises in Russia are extremely limited. In fact, the making of profits by buying and selling goods is strictly forbidden. Thus, an overwhelmingly large part of the national income available for consumption in Russia is distributed in the form of wages, as should be the case according to the prospectus of modern socialism.

*Wages in Russia.* Payments which are officially recognized as wages are incorporated in the economic plans of the Russian economy. That is, the economic plans specify a certain total sum or fund which is to be used for wage payments in a given year and indicate how this fund is to be allocated among the various industries and individual enterprises of the country. Each industry and each enterprise thus knows in advance how much money it may pay out in wages during each year. The government also sets up minimum rates of wages for various classes of workers and establishes piece rates for various operations. The total wage fund increased from 8 billion rubles in 1928 to 32.7 billion rubles in 1932, 82.2 billion rubles in 1937, and a planned 133.2 billion rubles in 1942.<sup>3</sup> The wage fund actually hit 123.7 billion rubles in 1940 and is supposed to increase to 201 billion rubles in 1950 under the Fourth Five-Year Plan.<sup>4</sup> The wage fund has increased much more rapidly than the number of workers receiving their wages from the fund, and the average money wage among these workers increased from 703 rubles

<sup>3</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 344.

<sup>4</sup> *International Conciliation*, April, 1948, p. 271.

in 1928 to over 4000 rubles per year in 1940. It is scheduled to reach 6000 rubles in 1950.<sup>5</sup>

While wages are determined by governmental action in Russia rather than by the free play of market forces, they have the usual two functional aspects. That is, on the one hand, wages are a reward for accomplishment in production and an incentive to continued productive activity. On the other hand, they constitute a device for evoking a distribution of labor among the various occupations and industries of the country which is appropriate for the carrying out of the economic plans. Both functions call for differences in wages rather than equal wages for all workers, but only under the most ideal conditions would a given set of wage differentials be perfectly suited to both purposes. Actually, if the planners set up wage differentials which will reward the workers accurately for their productivity in all lines of work, in so far as the planners can determine productivity, they may find nevertheless that they have too many workers in some occupations and industries and too few in others. Conversely, the set of wage differentials which will produce a distribution of workers among occupations and industries which is suitable for the carrying out of the economic plans may give some workers more and other workers less than they deserve according to the planners' notions of the relative values of the various products of labor. The planners aim in general to reward the workers on the basis of productivity, but we must remember that productivity in Russia is not the same thing as it is in capitalistic economies, for the values of workers' products which are so important in estimating the values of the workers' services are determined in Russia by the decisions of the planners and not by the free play of demand and supply forces in the market. Since the values of the workers' products are arbitrarily determined and since the emphasis in Russia is always on plan-fulfillment, it is probable that the desire to reward the workers strictly on the basis of their accomplishment would give way, if necessary, to the desire to distribute the workers among occupations and industries so that the plans could be fulfilled as nearly as possible.

*Inequality in Russia.* Since practically all the Russian national income is distributed directly or indirectly in the form of wages, the existence of differences in wages produces a moderate degree of inequality in the distribution of the national income. The wage

<sup>5</sup> *Ibid.*

differentials have always been set up on a more or less experimental basis and have been subject to frequent and considerable changes. In the early days after the period of War Communism, it was intended that the highest wages should only be about three times as great as the lowest. By the end of the First Five-Year Plan, the ratio between the highest and lowest money wages was commonly reported to be about 10 to 1. This ratio was reported to be about 12 to 1 in 1937.<sup>6</sup> A decree of November, 1937, established a minimum wage of 110 rubles per month for workers in industry and transportation and a further decree of August, 1938, prohibited salaries above 2000 rubles per month. On this basis, the extent of inequality in incomes for workers of all grades in industry and transportation was about 18 to 1.<sup>7</sup> Inequality over the whole economy was somewhat greater than this, for some workers in other fields undoubtedly received wages which were below the minimum established for workers in industry and transportation. A still later prewar estimate indicated that the extent of inequality in income distribution in Russia, as measured by the highest and lowest wages, was about 20 to 1.<sup>8</sup> Even inequality on the order of about 20 to 1 was, of course, extremely small in comparison with that which prevails in capitalistic countries where the ratio between the highest and lowest incomes is several thousand to one (some socialists say 40,000 to 1 in the United States).

Critics of the Russian economy sometimes alleged that these officially admitted differences in wages and income did not tell the whole story and that high party and industrial officials drew salaries which were far above the legal maximum. Sometimes, these critics said with bated breath, these fortunate individuals received as much as 7000 rubles a month. On the basis of the minimum wage for workers in industry and transportation, this would have produced inequality of something like 64 to 1 between the highest and lowest incomes. There was no way of proving or disproving such claims but, in order to avoid becoming too enthusiastic about them, we may point out that an income of 7000 rubles per month, even at the official rate of exchange, would have been the equivalent of only about \$16,800 per year. Now that is a good-sized income, but many of our capitalists, who liked to talk about the great inequality

<sup>6</sup> *The Nation*, November 13, 1937, pp. 523-526.

<sup>7</sup> M. T. Florinsky, *Toward an Understanding of the USSR*, p. 168.

<sup>8</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 165.

which prevailed in the distribution of income in Soviet Russia, would have thought that our capitalistic system had been ruined if the top incomes had been limited to \$16,800 per year, even after taxation.

Inequality in the distribution of money income takes no account of the various social services which are distributed to the Russian citizens from time to time. Sometimes it is claimed that the citizens receive as much as a fourth of their real income in the form of social services and free public services which are enjoyed more or less on the basis of need.<sup>9</sup> If these items are distributed rather equally among persons with large and small money incomes, they operate to make the extent of inequality in the distribution of real income considerably less than that in the distribution of money income. On the other hand, some critics contend that various free services are distributed in such a way as to make inequality in the distribution of real income actually greater than that in the distribution of money income. That is, they say that the persons who draw the largest salaries are also granted the free use of magnificent houses or apartments, country estates, rest homes and sanatoria, expensive limousines, and many other things to which ordinary citizens have no access. Once again, we have no way of evaluating these conflicting claims.

During World War II, much was heard about increased emphasis on differential wages and salaries as a means of stimulating worker productivity in the Soviet Russian system. By the beginning of 1947, when the average wage of workers in the national economy was probably about 450 rubles per month, outstanding individual workers were receiving 4000 to 5000 rubles per month, and plant directors, high officials, leading scientists, and other select groups made as high as 6000 rubles per month.<sup>10</sup> Such differences in wages between the average workers and the highest-paid workers meant, of course, much larger differentials between the highest-paid and the lowest-paid workers. And if, as commonly rumored, the highest-paid workers receive especially wonderful grants of "free" services and commodities directly from the government in addition to their money pay, inequality in the distribution of real income in Soviet Russia may now bear at least a family resemblance to that which exists under capitalism after taxation.

<sup>9</sup> John Strachey, *How Socialism Works*, p. 159.

<sup>10</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 79.

*Incentives in Russia* The wage system of Soviet Russia indicates that the leaders of the economy intend to depend quite strongly on the economic motivation of workers of all grades as a means of achieving efficiency and increased productivity In as many types of work as possible, wage payments are on a piecework basis And the piecework system in Russia is in a position to furnish a strong stimulus to the workers since there are no capitalistic employers to lower the piece rates as soon as the workers begin to make a little more money than usual and to bring about a situation in which the workers will have to work much harder than formerly to earn even their former wages However, the Russians have attempted to use the piecework basis of wage payment for some types of work which in other countries would not be considered well suited for this system, such as, for example, repair work and work requiring great precision The piecework system has sometimes led to the turning out of large quantities of low-quality product, to an unduly large amount of overtime work, and to a failure to use safeguards for workers in cases where such devices would lower the speed at which work could be carried on.

Additional bonuses beyond ordinary piecework earnings are widely used to reward Russian workers who greatly increase the quality and quantity of their work The increases which have occurred in wage differentials from time to time indicate the willingness of the leaders to experiment with the wage system and to make any concessions within reason to induce the workers to put forth their best efforts and increase productivity On the other hand, the increasing average money wages of the Russian workers have not been matched by similar increases in real wages, and this fact has doubtless robbed the increases in money wages of much of their effectiveness in stimulating the workers The Russian workers are relieved of many of the worries which beset the workers of capitalistic countries That is, there is no danger of their being unable to find work and there is, as we shall see in a later chapter, an adequate system of social insurance to provide against the other risks to which workers are especially subject The Russian workers also have an opportunity to move up and advance from a low-paying job to one with a higher rating and more adequate compensation If they think they can qualify for the higher job, they declare their intention of doing that type of work and must be given a two weeks' trial

at it. Of course, they fall back if they fail, but otherwise the better job and its remuneration are theirs.

In the Russian system, economic rewards are often combined judiciously with public honors and prestige values. For example, exceptionally productive workers are sometimes made "Heroes of Socialist Toil," a title which carries with it a great amount of honor and prestige (including automatically the award of the Order of Lenin, Russia's highest decoration) and also such advantages as additional compensation, free street-car service and passes for travel, and preferential housing. Other valiant workers are given the medals "For Prowess in Labor" or "For Distinguished Labor," which involve lower-grade honors and smaller material advantages. "Stalin Prizes" to the value of 100,000, 50,000, and 20,000 rubles, are also awarded for outstanding material and cultural achievements.

A similar combination of public honors and economic advantages was used by the Russian leaders in their sponsorship of the famous Stakhanovite movement. It was on August 31, 1935, that the coal miner, Alexei Stakhanov, produced 102 tons of coal in a six-hour day, instead of the usual quota of 6 to 7 tons. As a result of this prodigious feat, he earned 225 rubles in one day and at the same time became a sort of social lion. His accomplishment was widely publicized, countless honors were bestowed upon him, and other workers in the same and other fields of economic activity were urged to do likewise. And they did. By October, 1935, another miner, Andrei Gorbatink, produced no less than 405 tons of coal in one day. A worker in shoe-manufacturing performed his operation on 1820 pairs of shoes in one day instead of the usual 680, a brick-layer laid 6554 bricks in a  $7\frac{1}{2}$ -hour day, workers in weaving began to tend 216 looms each instead of the standard 26, and so on.<sup>11</sup> At the moment, we are not interested in analyzing all the good and bad effects of Stakhanovism but merely in pointing out that the exceptionally productive workers were rewarded both with greatly increased earnings and with public acclaim and notoriety.

Many other public honors await the performance of conspicuous feats of productivity by the workers. Pictures of outstanding workers may be hung upon factory walls, busts may be set up in convenient places about the plant, and favorable comment by the Soviet press is common. Some workers have been rewarded with trips to Moscow which have included opportunities to meet and be

<sup>11</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 189.

congratulated by the big boss of all the Russians. What is called "socialist competition" is also relied upon to stimulate the workers. The aim of socialist competition is to make a game or contest out of such mundane occupations as ploughing fields, manufacturing shoes, or laying bricks. Gangs of workers compete to maximize output or minimize breakage, waste, and scrap. After the contests, mutual aid is supposed to be the order of the day, with the winners helping the losers to increase their efficiency. The Russian system also appeals to idealism, altruism, and devotion to the cause. Workers are expected to devote a part of their free time to voluntary labor and to undertake some task without compensation in addition to their regular work. Finally, of course, the workers may be stimulated by pride in their work, by the realization that they are part-owners and part-managers as well as workers, and by their opportunities to suggest improvements and changes in methods.

On the other side of the picture are various negative incentives. The Russian workers are under ultimate compulsion to work if they desire to be consumers. Unsatisfactory work may draw dishonorable mention in factory newspapers or wall placards, and tipsy workers may have to draw their pay at special bottle-shaped windows for habitual drinkers. Courts of workers have been used to deal with a number of offenses of workers, such as habitual lateness, soldiering on the job, coming to work in an intoxicated condition, undue shifting of jobs, careless and neglectful treatment of socialist property, faulty work, and waste of material. In recent years, the continuation of many of these evils has led the government to take drastic direct action to reduce or eliminate them, as we shall see at a later point.

The Russian system of economic and non-economic incentives for workers would seem at first glance to be adequate, but the results do not always bear out this conclusion. That is, as we have suggested previously, the efficiency and productivity of Russian workers of all grades remain low in spite of all incentives and inducements. For example, at the end of the Second Five-Year Plan, it was not some carping outside critic but a special committee of the State Planning Commission that estimated the average labor productivity throughout all Russian industries to be only 40.5 per cent of that of the United States. And this was the case even though average labor productivity in Russia had increased by 82 per cent during the Second

Five-Year Plan<sup>12</sup> At the same time, the average production of coal per worker in Russia was 970 tons as compared with 844 tons per worker in the United States. The amount of cast iron per blast furnace worker was 756 tons in Russia and 1260 tons in the United States.<sup>13</sup> Russian plants in various manufacturing industries often required two or three times as many workers of all sorts as did American plants of similar general size and output.

Labor productivity in large-scale industry in Russia had increased by another 38 per cent by 1940.<sup>14</sup> During the period of World War II, under the unusual stimuli operating at the time, labor productivity in Russia was kept at a surprisingly high level, especially in view of the fact that large numbers of workers were lost to the armed forces or to the enemy and had to be replaced with youths, housewives, and old men. However, the postwar situation was much less favorable, at least in the early years. During 1946, labor productivity was thought to be "well below the prewar level, not only because of the normal disruption of production caused by large-scale reconversion, but also because of the poor condition of factories and machines in the devastated western area, the wearing out of much of the machinery in the eastern U.S.S.R., and probably also the weariness of Soviet workers after the privations and exertions of one of the most bitter struggles in history."<sup>15</sup>

The general question, is, of course, whether the low efficiency of Russian labor must be charged to inadequacy of the system of incentives or whether it is due to other factors, and this question cannot be definitely answered as yet. The inefficiency and low productivity of labor may be due in part to the rapidity with which the Russian economy has been industrialized and mechanized. When large numbers of workers from the treeless plains, who have never seen an axe let alone a machine, are brought into mines and factories and set to work with modern complicated industrial machinery and equipment, it is unreasonable to expect anything except inefficiency and low productivity under any system of incentives. Of course, any given batch of workers will eventually become trained, or at least experienced, but the Russian labor force in industry has been growing very rapidly, and there has never been a time when this labor force as a whole could be considered properly trained and experi-

<sup>12</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 345.

<sup>13</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 184.

<sup>14</sup> A. Baykov, *op. cit.*, p. 345.

<sup>15</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 76.

enced Russian workers have found it difficult to adjust themselves to the strict regimen of urban industrial life, and they have been inclined to be late for work, to miss work altogether if they wanted to do something else on a given day, to take it easy on the job, to disregard safety rules, and to be careless in the use of materials and equipment.

Conscious of a general shortage of labor in industry and certain that they could get a job almost anywhere, the workers have been disposed to change jobs frequently and to move from one place to another in search of greener pastures. Labor turnover in Russia has been simply amazing. In some individual plants, there has been a complete change of personnel, office employees as well as ordinary workers, as often as two or three times a year. In one year, over the whole economy, 176.4 per cent of the average number of workers on the payrolls were hired, and 152.4 per cent quit work.<sup>16</sup> This problem has carried over into the postwar period, with large numbers of Soviet workers shifting jobs frequently in search of better conditions of housing, food, and work. Rapid labor turnover is costly in itself and has a destructive effect on the productivity of labor.

Again, low productivity of ordinary workers has been due in part to the inefficiency of management. The operation of factories has been characterized by a lack of balance and coordination and a failure to plan the whole order of work. Breakdowns have occurred all too frequently. All these difficulties may turn out in the long run to be nothing more serious than growing pains associated with the comparative youth of the Russian industrial economy. If they disappear and the level of labor productivity improves to something like that prevailing in other industrial countries, there will be little reason to question the adequacy of the Russian system of incentives. However, if labor efficiency and productivity remain low after, say, a generation of experience with the industrialized economy, we shall need to be very doubtful concerning the effectiveness of the Russian system of incentives.

#### *The Distribution of Income in Britain under Partial Socialism*

**Functional Distribution** The coming of partial socialism in Britain has brought little change in the distribution of income on a

<sup>16</sup> A. Yugow, *op. cit.*, p. 174.

functional basis. Individuals may still receive rent for the use of their land and interest on the capital funds which they have invested in various productive projects. Some industries have been nationalized, to be sure, but then former owners have been compensated for the loss of their properties and, in some cases at least, the compensation has been such as to insure that these owners will receive about the same annual incomes as formerly. Outside of the nationalized industries, private enterprises are still allowed to make profits if they are able to do so under the many economic controls which the government has imposed. And, of course, wages and

TABLE 18

*FUNCTIONAL DISTRIBUTION OF THE NATIONAL INCOME IN BRITAIN*  
(In £ Millions)

Type of Income	1938	1945	1946
Rent of land and buildings	380	385	386
Interest and profits	1368	2390	2370
Salaries	1110	1530	1675
Wages	1735	2780	3020
Pay and allowances of armed forces	78	1255	523
Total income	4671	8340	7974

SOURCE: *Statistics on Britain's Position*, February, 1948, p. 30.

salaries are paid and received as usual. The data in Table 18 give an indication of the functional distribution of the British national income in 1946 as compared with 1938 and 1945.

*Inequality in Britain.* By 1946, partial socialism in Britain had brought no great diversion of income toward the workers of the economy. Wages, salaries, and the pay and allowances of the armed forces made up 65.4 per cent of the total national income in 1946, as compared with 62.6 per cent in 1938, and even this slight change probably would not have occurred if rents had not been almost completely stabilized under governmental control during the war and postwar period. The part of the national income going to the workers in Britain in 1946 was almost exactly the same as in the United States. Inequality in the distribution of income on a personal or family basis, before taxation, was probably somewhat greater in Britain than in the United States. That is, Britain, being an older country, had had more time for the institution of inheritance to get in its work and probably had a considerably greater

concentration of the ownership of wealth than did the United States

After taxation, inequality in the distribution of income is probably somewhat less in Britain than in the United States. The basic rate of the British income tax is 45 per cent of taxable income, though lower rates of 15 and 30 per cent apply to the first small amounts of taxable income. Besides the basic rate, there is a surtax which begins at 10 per cent on the first eligible £500 and runs up to a maximum of 52.5 per cent. At this maximum rate, the income covered is paying total income tax and surtax of 97.5 per cent. In addition to the income tax and other taxes, Britain now has a special levy on investment income. It applies only when the taxpayer's total income exceeds £2000 and his investment income exceeds £250. The rate is 10 per cent on the slice of investment income between £250 and £500 and rises to a maximum of 50 per cent on income exceeding £5000.<sup>17</sup> The combination of basic income tax, surtax, and special investment levy can clearly run well above 100 per cent on parts of the income of considerable numbers of people. Such taxes operate to reduce sharply the inequality which would otherwise exist in the distribution of income.

*Incentives in Britain* The problem of incentives in Britain is a troublesome one at the present time. Production in many fields has recovered sharply since the war, is now well above prewar levels, and has exceeded the goals set up by the Labor Government. In other lines, however, production has been lagging, is still short of prewar levels, and has failed to hit the targets set up for it by the government. On the whole, it must be confessed that Britain in 1948 was still unable to work out her own economic salvation and was still dependent to a considerable extent on outside help, which came very largely from the United States.

In this situation, it is rather difficult to determine what has happened to labor productivity in Britain, but at least two studies have concluded that little or nothing has happened on the average and that labor productivity or output per man-hour is still just about what it was before the war.<sup>18</sup> Such a result, considered by itself, would not be very favorable. The question would still remain, however, as to whether the result was due to an unsatisfactory system

<sup>17</sup> *Britain's Budget* New York: British Information Services, 1948, pp. 34.

<sup>18</sup> *Labor and Industry in Britain*, March, 1948, pp. 12-15.

of incentives or some other factor affecting workers of all grades, or to events wholly beyond the workers' control

There is one school of thought which holds that Britain has no satisfactory system of incentives under partial socialism, that confiscatory taxation and stringent government controls prevent the usual capitalistic system of incentives from operating successfully, and that the Labor Government does not have or does not care to use powers of compulsion to stimulate the workers to greater productivity. According to this point of view, Britain will have to go backward toward more capitalistic methods of operation or forward to more complete socialism, with the probability favoring the latter course of action, if satisfactory progress in regard to labor productivity is to be attained.

It is true, of course, that workers are rather well treated in most respects in socialist Britain. They still have their unions and make use of collective bargaining to settle issues with the employers. The government does not hesitate to control prices directly, but it merely asks that wages be frozen voluntarily at existing levels in order to prevent inflation and higher costs. There is very little unemployment in Britain and the prevention of unemployment is one of the major objectives of the Labor Government. And the workers are covered by a most extensive system of social insurance and are benefited by a variety of social services. Whether all these things will operate in the long run to increase or to reduce labor efforts and productivity cannot be determined in advance.

### *The Distribution of Income under Fascism*

**The General Situation.** The economic institutions of Italy and Germany under fascism were nominally those of capitalistic economies. Land and capital were owned by private individuals for the most part, many industries were privately owned and operated, economic activity was at least partly competitive, and all of the familiar shares in income distribution which we know under capitalism were present. On this basis, it might be thought that our general theories of distribution would be as valid for fascism as for capitalism, but this conclusion was not really warranted. In the fascist countries, the leaders of party and government were free to interfere with and control economic activity to any desired extent, and their powers extended quite naturally to the division of the national income.

They were quite capable of ordering business enterprises to invest all earnings, above a certain rather meager rate, in government bonds, of placing prohibitive taxes on dividend payments so as to force businesses to reinvest their earnings, of ordering general changes in wages and prices throughout the economic system, of limiting the rents which could be charged, or of placing burdensome capital levies on the value of land or the capital and surplus of corporations.

Thus, while rent, interest, wages, and profits existed as shares of income for private individuals in the fascist countries, the only principle that can be advanced in connection with these distributive shares is that they were whatever the leaders of party and government wanted them to be, which is the same as having no principle at all. Even if the leaders had permitted a considerable part, say half or more, of the fields of economic activity to operate without direct governmental interference, our theories of distribution would not have been valid even for this unrestricted section of the economy. That is, it would not have been possible to make the distributive shares in this free sector of the economy entirely independent of the conditions which prevailed in the controlled section of the economy. The conclusion is, therefore, that the extent of governmental interference with economic activity under fascism was always too great to permit the general theories of distribution—which depend, among other things, on the markets for the productive agents being free of governmental interference and control—to be even roughly applicable.

*The Distributive Shares.* There was nothing about the fascist regimes in Germany and Italy which tended to divert a larger share of the national income in the direction of the workers. In fact, the trend was apparently in the other direction. In Germany, for example, wages, salaries, and other earned incomes amounted to 77.4 per cent of the total national income in 1932, while property incomes (including profits, undistributed profits, interest and dividends, and rent) absorbed 19.1 per cent of the total. By 1938, the share going to wages, salaries, and other earned income had declined to 63.7 per cent of the total national income, while property incomes had increased to 28.0 per cent of the total.<sup>10</sup> Now it might be objected that these results are only what should be expected as between a year of deep depression and one of relative prosperity, and that they show

<sup>10</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 208.

little if anything concerning the effects of the policies of fascism. However, this objection may be answered by pointing out that wages, salaries, and other earned incomes took 51 per cent less of the national income in 1938 than in 1929, while the share going to property incomes was 59 per cent greater in 1938 than in 1929.<sup>20</sup>

Apparently, then, the fascist regime in Germany took much better care of enterprisers and rentiers than of workers. And the enterprisers fared best of all, for profits and undistributed profits took 22.9 per cent of the national income in 1938, as compared with 11.3 per cent in 1932 and 16.7 per cent in 1929.<sup>21</sup> Over the entire period from 1932 through 1938, the total of property incomes increased by 146.4 per cent. In the same period, total income from wages and salaries increased by only 66.1 per cent, in spite of a 55.2 per cent increase in the total number of employed workers, a 117 per cent increase in the total hours worked in industry, and a large increase in the total volume of production.<sup>22</sup> Nor was the income position of the workers much better when account was taken of the relative tax burden. The ordinary German worker was spending about 22 per cent of his income for taxes and various "voluntary" and compulsory contributions, while these items on the whole made up about a third of the national income.<sup>23</sup>

However, the workers were relatively sure of having employment in the later years of the fascist regimes, and they had the benefit of a long established system of social insurance. They were allowed to participate in vacation trips, concerts, theater performances, sports, and many other cultural, educational, and recreational activities through the "Strength through Joy" department of the Labor Front in Germany and the *Opera Nazionale Dopolavoro* in Italy, and in Germany the Labor Front, through its Beauty of Work movement, spent some money to try to assure the workers of happy, beautiful work-places.

*Inequality in the Distribution of Income.* The national income was distributed very unequally among individuals and families in the fascist countries. In Germany, for example, out of more than 30,000,000 individual income receivers in 1936, there were about 15,000,000 who received less than 1200 marks per year, and another

<sup>20</sup> *Ibid.*

<sup>21</sup> F. L. Neumann *Behemoth. The Structure and Practice of National Socialism*, p. 436.

<sup>22</sup> *Ibid.*

<sup>23</sup> M. Y. Sweczy, *The Structure of the Nazi Economy*, p. 209.

11,500,000 who received incomes ranging from 1200 to 3000 marks. At the other end of the scale, there were 5000 individuals with incomes of 100,000 marks or over, 18,000 individuals with incomes of 50,000 to 100,000 marks, 57,000 individuals with incomes of 25,000 to 50,000 marks, and 119,000 individuals with incomes of 16,000 to 25,000 marks.<sup>24</sup> Moreover, inequality in the distribution of income increased apparently under the auspices of German fascism. According to Sweezy, the coefficient of average inequality, computed in such a way that an increase in the coefficient indicates an increase in inequality in the distribution of income, was 0.599 for 1936, as compared with 0.500 in 1932 and 0.552 in 1928.<sup>25</sup> On the whole, however, national income appeared to be more equally distributed in Germany than in the United States.

Even among the wage-earners, inequality apparently increased in Germany under fascism. In 1929, only about 16 per cent of the total number of wage-earners received less than 12 marks per week, while in 1938 some 22 per cent of the wage-earners were in this category. The percentage of wage-earners receiving over 30 marks per week was about the same in both years.<sup>26</sup> Clearly there was a relative thinning out of the wage-earners in the middle brackets over this period. There was also great inequality in the distribution of wealth in Germany. Without going into great details, we may say that the coefficient of average inequality was 0.649 in 1931 and 0.721 in 1935. Thus, in Germany as in capitalistic countries, inequality in the distribution of wealth was greater than inequality in the distribution of income.<sup>27</sup>

In closely controlled economies, such as those of the fascist countries, the importance of inequality in the distribution of income was not so great as in a capitalistic economy which operates more or less automatically on the basis of the price mechanism and the market. That is, the evil effects of inequality could be minimized or in some cases eliminated, by governmental control over the uses to which money incomes could be put. And, during World War II, with the government taking a large proportion of the national income for its own purposes, it probably made comparatively little difference how the national income was divided among individuals in the first place. On the other hand, it cannot be denied that the distribution of wealth and income in the fascist countries was much more nearly capitalistic than anything else, and that the inequality

<sup>24</sup> *Ibid.*, p. 212

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*, p. 216

<sup>27</sup> *Ibid.*, p. 218

which prevailed fitted in very poorly with the contentions of the fascist leaders that the desires of the citizens for economic gains should be subordinated to such intangibles as national pride and glory, racial purity, sanctity, heroism, idealism, and devotion to the cause.

### QUESTIONS

- 1 What do the socialists mean when they say that rent, interest, and profits would be eliminated under modern socialism? Explain
- 2 'Even if it were considered desirable, an equal distribution of income under socialism would be very difficult to achieve' Show whether you agree
- 3 "Differentials in wages under socialism, even though they were paid on the basis of productivity, would be much smaller than those which exist in our capitalistic system" Explain
- 4 How great a degree of inequality in the distribution of income would a system of modern socialism probably tolerate? Explain
- 5 Would the differences in incomes which modern socialism contemplates be adequate to provide incentives for all? Explain
- 6 'A socialist system would not rely entirely on differences in wages to provide incentives for the people' Explain
- 7 "The distribution of income under ideal communism would be exceedingly simple" Do you agree? Explain
- 8 "Soviet Russia has not succeeded in entirely eliminating property incomes" Show whether you agree
- 9 Do differences in wages in Soviet Russia depend primarily on the desire to reward the workers strictly on the basis of their productivity or on the desire to distribute the workers among occupations and industries so that the economic plans can be fulfilled as nearly as possible? Explain
- 10 "Inequality in the distribution of income in Soviet Russia is almost as great as that which exists in leading capitalistic countries" Show whether you agree
- 11 To what extent does Soviet Russia employ non wage incentives to get things done? Explain
- 12 'The low efficiency and productivity of the workers indicate that the Soviet Russian system of economic and non economic incentives for workers is inadequate' Do you agree? Explain
- 13 "The distribution of income in Soviet Russia was not affected by the developments of World War II" Show whether you agree
- 14 "The coming of partial socialism in Britain has brought little change in the distribution of income on a functional basis" Explain
- 15 "In discussing inequality in the distribution of income in Britain, it makes a great deal of difference whether one is speaking of inequality before taxation or after taxation" Do you agree? Explain

- 16 "There is every reason to think that incentives for workers in Britain have remained adequate under partial socialism" Discuss
- 17 "There were really no economic principles which controlled the final distribution of income among persons under fascism" Show whether you agree
- 18 "The unsocialistic character of National Socialism was clearly indicated by the statistics on the general shares of the national income in Germany" Explain
- 19 "There is little reason to believe that the extent of inequality in the distribution of income in Germany and Italy under fascism differed sharply from that which exists in capitalistic countries" Do you agree? Explain
- 20 "In closely controlled economies such as those of the fascist countries, the importance of inequality in the distribution of income is not so great as in a capitalistic economy" Explain

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## CHAPTER 17

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### THE STATUS OF LABOR

#### *The Status of Labor under Capitalism*

**Wages, Hours, and Working Conditions** Since workers and their families make up a large part of the population of any economic system, the status of labor in the various types of economic systems is an important topic for consideration in comparing and evaluating these systems Under pure capitalism, wages, hours, and other working conditions are supposed to be the result of the operation of market forces The workers compete actively for employment and the employers compete actively for the workers and, under such conditions of perfect competition, the results are supposed to be not only satisfactory hours and working conditions for the workers but also wages which measure very accurately the marginal contributions of the workers to product-value There should be no need for governmental interference in these matters, for unions or organizations of workers and employers, or for government-sponsored systems of social security There should be no unemployment and the government should have no policy with respect to the matter of population growth

In actually operating capitalistic systems, conditions of perfect competition are seldom if ever present in the markets for labor Individual workers and groups of workers differ sharply with respect to bargaining power, mobility as between places and occupations, and other matters which affect the terms of employment The competition of employers for workers and of workers for employment is sometimes active and sometimes not Under these conditions, great disparities exist between workers and groups of workers with respect to wages, hours of work, and other conditions of employment Moreover, the federal government and other govern-

mental units interfere quite frequently in matters affecting the status of labor.

*Wages, Hours, and Working Conditions in the United States* In the United States, there were about 61,296,000 gainfully employed persons in the middle of 1948. Included in the total number of employees were some 16,058,000 in manufacturing, 9,648,000 in trade, 9,396,000 in agriculture, 5,607,000 governmental employees, 4,663,000 in service fields, 4,092,000 in transportation and public utilities, 2,182,000 in construction, and 1,727,000 in finance.<sup>1</sup> At the same time, average weekly earnings in all manufacturing industries amounted to \$52.81, which would give an annual rate of about \$2746. Such average figures mean comparatively little, for they cover up great disparities in wages from one field to another in manufacturing and among the individual workers in the various fields. For example, average weekly earnings in manufacturing in May, 1948, varied between \$37.12 and \$72.78 from the lowest to the highest field.<sup>2</sup> Variations in wages were even wider when non-manufacturing fields were included in the picture.

The traditional wages on a time basis, or so much per hour or day, are still widely used in American industry, but firms in some industries use various kinds of incentive wage systems which afford the workers additional earnings when they increase the quantity of their work while maintaining quality. In many years, the existence of considerable though varying numbers of unemployed workers gives the workers who have jobs an incentive to maintain at least fair efficiency lest they be denied access to the material agents of production and be made to exchange places with unemployed workers. Under such conditions, employers themselves are able to deal quite effectively with such problems as absenteeism, lateness to work, and undue labor turnover. However, some of these problems have been more troublesome than usual under the conditions of full employment which have prevailed during the war and early postwar periods. In the more distant past, comparatively few ordinary workers in American industries have been able to command adequate annual vacations with pay, but in the last few years this situation has been changed in a large number of fields.

The average actual working week of the employees in all manufacturing industries in the United States was 39.8 hours in May,

<sup>1</sup> *Survey of Current Business*, August, 1948, p. S-9.

<sup>2</sup> *Ibid.*, pp. S 13, 14.

1948, but the variations were from 34.2 to 46.7 hours in different manufacturing fields. In non-manufacturing fields (not including agriculture), the average weekly hours per worker varied from 37.2 in building construction to 46.5 in the operation of street railways and busses.<sup>3</sup> Great disparities also exist in the working conditions under which the workers are employed. Some work places are sanitary, and well lighted, heated, and ventilated, while others are miserable in the extreme. Thus, the general picture with respect to wages, hours, and working conditions is one of extreme inequality. Some workers receive high wages or salaries for working short hours under ideal working conditions, while others receive mere pittances for slaving long hours under abominable working conditions.

*Governmental Interference.* The citizens of the United States as a group have not always been willing to accept the wages, hours, and working conditions produced by the operation of market forces as entirely satisfactory. As a result, the federal government and other units of government have come to interfere with these results in a variety of ways. For example, the economy has been operating since 1938 under the influence of the Fair Labor Standards Act, which aimed to put a floor under wages and a ceiling over hours. The Act forbade employers whose products move in interstate commerce to pay wages of less than 25 cents per hour, or to work their employees more than forty-four hours per week unless they were willing to pay overtime wages in cash at the rate of "time and a half." The Act also provided for a gradual increase in wages and decrease in hours through time until, by 1945, the minimum wage would be 40 cents an hour and the maximum hours would be forty a week.

While the minimum wages originally provided by the Act were only \$11 per week for a forty-four hour week, it was estimated that the Act affected immediately some 750,000 workers with respect to wages and 1,500,000 in the matter of hours.<sup>4</sup> As the maximum hours decreased and the minimum wages increased, it was expected that some 11,000,000 workers would eventually benefit. The widespread increases in wages which occurred during the war and early postwar periods upset this latter calculation considerably, and the rapidly rising prices of consumable goods made the minimum wages pro-

<sup>3</sup> *Ibid.*, pp. 512, 13.

<sup>4</sup> P. F. Gemmill and R. H. Blodgett, *Economics: Principles and Problems*. New York: Harper and Brothers, 1948, p. 427.

vided by the Act entirely inadequate in any case Increases in the minimum wages have been recommended to Congress on several occasions, but they had not been enacted up to the middle of 1949

The Fair Labor Standards Act of 1938 also attempted to deal with the problem of child labor and it provided that, in industries engaged in interstate commerce, no child under sixteen years of age could be employed None under eighteen years of age could be employed if the work was hazardous or unhealthy It was high time that something was done about the problem of child labor, for in previous years more than 2,000,000 children from 10 to 17 years of age were gainfully employed in the United States and often with the most unfortunate results However, the federal government had made several previous attempts to regulate and control the use of child labor On three separate occasions, federal laws dealing with this matter had been declared unconstitutional by the Supreme Court of the United States, and a constitutional amendment for the same general purpose had failed of ratification by the states The federal government has also interfered with the natural operation of labor markets by means of legislation promoting and fostering the organization and development of labor unions, as we shall see later Finally, state governments have interfered with wages, hours, and working conditions for particular groups of workers by means of legislation

*Labor Unions under Capitalism* The workers of capitalistic countries in general and of the United States in particular have not been content to rely entirely on governmental intervention for the improvement of their economic status Instead, they have banded themselves together into labor unions for the purpose of bargaining collectively with the employers The individual worker is usually at a great disadvantage in bargaining with the employer His services are perishable and must be sold from day to day, and he does not usually have financial reserves which are large enough to permit him to hold out very long for better terms of employment On the other hand, while the employer must have employees, one worker more or less means very little to him Under collective bargaining, the worker's disadvantage is eliminated or greatly reduced His need for a job is not reduced, but the question facing the employer becomes one of having a complete labor force or none at all, rather than one of having or not having a particular worker The workers, gathered together in a union and delegating the task of bargaining

with the employer to an official or agent of the union, can often obtain much better terms of employment than the individual workers could obtain for themselves.

Labor unions in the United States are of several kinds, but the two most important types are craft unions and industrial unions. A craft union is an organization of workers in a certain craft or trade (such as bricklaying or cigar-making), and it aims to promote the economic interests of this group of workers alone. An industrial union, on the other hand, aims to include all employees who work in a given plant or industry without regard for the types of work which they perform. Thus, it is often said that a craft union operates horizontally, since its membership may cut across many plants or even industries, while an industrial union operates vertically, since it aims to take in all workers, whether skilled or unskilled, in a plant or a whole industry. The chief function of wage-conscious labor unions is to bargain collectively with the employers to secure better terms of employment for the workers, union recognition, collective agreements, and closed shops, and if necessary, to use the weapons of organized labor, such as the strike and the boycott, on the employers. Many unions carry on also a variety of educational, recreational, social, and cultural activities for their members and some of them have provided certain forms of social insurance for their members in the past. On less frequent occasions, labor unions have been able to participate to some extent in the management of particular enterprises through union-management cooperation or other devices.

With some conspicuous exceptions, employers in the United States have been bitterly opposed to the growth and development of labor unions. They have thought that the development of unions would have an unfavorable effect on the earnings of their enterprises and would interfere with their so called right to manage their businesses as they chose, without interference from any "outside" agency. Their opposition has also been based in some cases on charges that the labor unions were radical and subversive and aimed at the eventual overthrow of the capitalistic system. It is difficult to regard this last contention as valid, unless one is inclined, as some employers are, to regard any request for an increase in wages as socialistic. While it cannot be doubted that some labor unions include radical elements, the unions in general seem to pursue capitalistic ends by capitalistic methods. Like the employers themselves,

they seek to achieve monopolies or quasi-monopolies and do not hesitate to restrict output if it seems probable that they can make more money in that way than by seeking to maximize production. In general, the unions have sought to prosper within the capitalistic system rather than by overthrowing it.

Many methods have been used by employers in the United States in combating the growth of labor unions. Many years ago, it was possible for employers to attack the budding unions in the courts under the conspiracy laws. The employers have insisted on the maintenance of the open shop in their plants and have sought to interfere with the development of the more vigorous types of labor unions by introducing an innocuous variety known as the "company union." The company union, which was ordinarily initiated and financed by the employer himself, contained representatives of both workers and management, did not usually deal with important questions such as those concerning wages, and could not be regarded as a genuine labor organization. Employers have frequently required their workers, as a condition of employment, to sign "yellow-dog" contracts under which the workers agreed not to join a labor union so long as they remained employees of the particular concerns, and sometimes agreed not to confer or associate with union organizers or members during their terms of employment. Labor injunctions, issued by willing judges, have also been widely used to interfere with the growth of labor unions. The labor injunctions were originally intended to protect the employers' property from irreparable damage during a strike or boycott, but came to be used to forbid non-union workers to join unions, to prevent picketing, the payment of strike benefits, or the publication of information concerning the progress of a labor dispute, and to keep union organizers from campaigning among the non-union employees of particular concerns. Employers have hired spies to associate with the workers, join their organizations, and report on their plans so that the employers would be able to resist them successfully. Employers have also hired armed thugs and bullies to beat up union organizers, ringleaders among the workers, or workers who were out on strike.

After interfering with some of these activities of employers from time to time, the federal government struck a telling blow for the labor movement in 1935 with the passage of the National Labor Relations Act. This law required employers to bargain collectively with representatives of their employees and prohibited employers

from carrying on unfair labor practices and from interfering in the organization of agencies for collective bargaining. The National Labor Relations Board was set up to administer the Act and was empowered to investigate and settle disputes, to issue orders to employers, and to have these orders enforced by the federal courts.

The Act was intended to stimulate the growth of labor organizations, and it seems to have had that effect in practice. The passage of the Act was followed by a great increase in union membership and the organization of labor in many plants and industries which had previously managed to escape organization. According to the best estimates available, there were around 14,500,000 union members in the United States at the end of 1947, including some 6,900,000 members of the American Federation of Labor and 6,000,000 members of the Congress of Industrial Organizations (CIO). When we deduct employers, business managers, self-employed persons, and agricultural workers from the total labor force, we find that about a third of the workers who might properly be termed "organizable" were members of unions. There were probably not over 5,000,000 union members when the Act was passed.

Though the constitutionality of the National Labor Relations Act was upheld by the Supreme Court in 1938, there were many employers and others who contended through the years that the Act had gone too far and had actually given labor the upper hand in dealing with the employers. The unsettled labor conditions of the early postwar period apparently convinced many members of Congress on this point, for the Labor-Management Relations (Taft-Hartley) Act was passed in 1947 to eliminate some specific abuses on the part of labor unions and to equalize bargaining conditions between unions and employers. Under the Act, no new closed-shop contracts may be made and the union shop (or closed shop with an open union) may be set up only if a majority of the workers in an establishment vote for it. The government may ask the courts for 80 day injunctions against strikes that affect the national safety. Jurisdictional strikes and secondary boycotts are prohibited in businesses in interstate commerce.

Unions as such are forbidden to make political contributions and expenditures, union-controlled health and welfare funds are prohibited, and unions are liable to suit for violations of contract. Before a strike may be called, workers must vote by secret ballot on

<sup>6</sup> *Ibid.*, pp. 407-408.

whether to accept the employer's final offer. An employer may discuss labor policies with his workers and may demand an election if he thinks the union no longer represents a majority of his employees. Unions may not charge dues or initiation fees deemed by the National Labor Relations Board to be excessive or discriminatory. The NLRB may not certify any union as a collective bargaining agent unless it has affidavits from the union officers stating that they are not communists. The NLRB has been enlarged to include five instead of three members and is to have a general counsel who will prosecute unfair labor practices.

*Wartime Labor Regulation.* During World War II, labor in the United States was subjected temporarily to rather rigorous governmental controls. Wages and salaries were frozen under the Anti-Inflation Act of 1942, and increases in rates of pay could be granted only under exceptional circumstances. A War Manpower Commission was set up and was given almost dictatorial authority over the people of the country. The Commission was empowered to decide who should work, where, and at what task, and whether he should or should not serve in the armed forces. By classifying occupations as essential or nonessential (and as deferrable or nondeferrable in their relation to active military service), by encouraging workers to shift from the latter to the former types of jobs, by specifying the conditions under which a worker might move from one job to another, and in other ways, the War Manpower Commission undertook to utilize the labor force of the country for expediting the prosecution of the war.

A National War Labor Board was established for the purpose of adjusting and settling labor disputes which might interrupt work which was contributing to the effective prosecution of the war. The NWLB consisted of four public members, four employer members, and four labor members (two representing the AFL and two the CIO). Regional War Labor Boards were set up, and disputes between employers and workers were heard by tripartite boards or panels, consisting of one representative each from industry, labor, and the public. Recommendations by these panels were made to the Regional Boards, which then rendered decisions that became effective except in cases in which appeals were taken to the National War Labor Board.

Since there were some actual strikes during the war period and threats of others in important fields of production, Congress also

enacted the War Labor Disputes (Smith-Connally) Act in 1943. The Act applied to establishments required for the war effort or useful in connection therewith. It authorized government seizure of private plants in which production had been interrupted by strikes and provided (1) for the maintenance of the same working conditions as prevailed prior to governmental possession and (2) for penalties against persons instigating or aiding any strike, slow-down, or interruption in plants taken over by the government. It also required that thirty days' notice of a labor dispute must be given, and that after the expiration of this waiting period a secret strike ballot should be conducted by the National Labor Relations Board for the purpose of determining whether a majority of the workers favored going on strike. Under all these types of governmental control, the status of labor in the United States during the war period seemed to differ only in degree from that of labor in Soviet Russia or Nazi Germany.

*Unemployment under Capitalism.* Since we are to compare labor conditions under capitalism with those which prevail in other types of economic systems, it seems desirable to state here the obvious fact that large numbers of potential workers sometimes find it impossible to obtain employment under the capitalistic system. Students of the problem usually distinguish at least three types of unemployment—technological, seasonal, and cyclical. While these three types of unemployment are rather closely interrelated and it is very difficult to divide the persons actually unemployed at any time into three watertight classes, it is clear that cyclical forces are of fundamental importance in connection with unemployment. At the worst of the post-1929 depression in the United States, some 14,500,000 workers, or roughly one-third of the available labor force, were unemployed, and at the peak of the following recovery period the number of unemployed never fell below 4,500,000. During the period of World War II, the demands of war production and the withdrawal of large numbers of workers into the armed forces combined to produce a temporary and most unsatisfactory solution for the unemployment problem. Unemployment was also at low ebb during the postwar boom period, but the problem remains one to be reckoned with in considering the general status of labor under capitalism.

In view of the importance of cyclical unemployment under capitalism, it is important to inquire whether the business cycles which

produce it are at all peculiar to capitalistic economies or whether they are likely to occur under all types of economic systems. While limitations of space will not even permit us to make a graceful bow in the direction of the many individual theories which have been concocted for explaining business cycles, we may suggest at this point that the former view seems more accurate than the latter. In other words, it seems to be the combination of modern methods of production and exchange with the institutions of capitalism, such as freedom of enterprise, private property, self-interest, competition, and the money and price system, which is responsible for the occurrence of business cycles. This, of course, is a claim which the socialists have been making for some time, and, whatever we may decide in connection with some of their other claims and theories, this one seems to contain a large element of truth.

The socialists contend that, in a system in which the control of economic activity as a whole is left in the hands of millions of private enterprisers, on the basis of freedom of enterprise, private property, and other capitalistic institutions, the total results of economic activity must inevitably be inappropriate to the social need from time to time. Individuals may plan their small parts of economic activity ever so carefully, but the total results are unplanned and the results obtained in different parts of the economy are uncoordinated. It is as if we were to set out to paint a great picture and gave each of a million individuals one square inch of canvas to execute as he pleased, subject to almost no restrictions as to design, colors, and other matters. When all the individual parts of the undertaking are completed, we put them together and call the result a picture. The total result may differ remarkably from that which we would have obtained if we had planned the whole picture before attempting to produce the individual parts, and may fit our real desires in the matter most indifferently. And yet the total results which are obtained by our economic system are produced in a fashion quite similar to the haphazard artistic venture just described, and naturally show, from time to time, lack of equilibrium and maladjustment.

Since the capitalistic system depends for its operation on the competitive activities of millions of individuals who are seeking to enlarge their incomes and follow their own self-interest, there is a strong tendency to overexpand economic activities from time to time. When the prices of goods are favorable and their production

is profitable, each individual enterpriser in competitive industries is likely to seek an increase in his income by enlarging production, assuming that, as a small fragment of the industry or economic system, he can take such action without reducing the price received for the product. When all or most enterprises in such industries react in this way, the tendency is for economic activities to be expanded to such an extent that a depression later on becomes unavoidable. Thus, it is alleged, under capitalism there is a tendency for competitive industries (at least) to overshoot the mark.

More important, according to socialists, is the fact that in a capitalistic economic system, with its private property, freedom of enterprise, and self-interest, there is a fundamental conflict between the interests of individuals and those of society as a whole—a conflict which stands out most clearly in the events of the business cycle. When, for example, a period of prosperity is well advanced, why does a depression occur? It is because the individuals in control of industry under the institution of private property are faced with the actual or prospective disappearance of "profits." Fearing that, if productive activities are continued as before, they will either fail to make money or will actually lose it, they decide to retrench, curtail production, discharge workers, stop buying materials and supplies, and so on. These activities cut down the incomes of workers, of farmers and of others who produce raw materials, of people who deal in materials, and so on. The declines in these money incomes operate to decrease the demand for all sorts of goods, including those sold in retail markets, and all industries feel the effects of the changed business conditions. The enterprisers and managers decide to retrench still further and make an additional cut in expenses, the money incomes of various classes of persons are again reduced, the demands for various economic goods again decline, productive operations are cut still further, and so on round and round.

Without bringing in the relationships between industries producing capital goods and those producing consumers' goods, or the financial and banking maladjustments which accompany declining production, we see that the efforts of business enterprisers to protect themselves operate cumulatively to produce the results which they feared. But what were society's interests at the time when the downward movement began? Clearly, with human wants large and rapidly growing, the interests of society as a whole demanded a continuation or even an expansion in the total of productive

activity If this conclusion seems doubtful, let us remember that, although some industries are said to be "overexpanded" in prosperity, the overexpansion is in relation to the possibility of sales at profitable prices and not in relation to the total quantities of the goods which the members of society desire

Getting back to the question of unemployment, we know that in depression large numbers of workers and large quantities of productive equipment stand idle Is this result desirable from the point of view of society's interests? If we recall that all our agents of production fully employed would be inadequate to produce enough goods to satisfy completely the wants of all the members of society, the answer is clear Why then do the productive agents remain idle? It is because our private enterprisers think that they cannot make profits by operating the productive equipment and by hiring the workers, and not because the goods which these agents of production could produce would not be eagerly consumed if the consumers could obtain them The conflict of interests is again apparent

*Full Employment Policy* The phenomenon of unemployment has made a tremendous impression on large numbers of people in our capitalistic system It has been a leading factor in causing some of them to conclude that we cannot afford to trust the future of our country to the automatic functioning of the capitalistic system, and that we must depend upon governmental direction and control This opinion is entitled to respect even from those who do not agree with it, for it seems to represent an honest choice between capitalism and the planned economy On the other hand, more people argue that we should retain our capitalistic system but that the federal government should assume responsibility for the successful operation of the system and especially for the maintenance of full employment This opinion is much more dubious, for it seems rather likely that the destruction of our capitalistic system might result from the operation of a full-employment policy by the government

The nature of a governmental policy for maintaining employment at a high level is clear enough When it appears that the aggregate demand resulting from private expenditures for consumption and investment plus normal governmental expenditures is going to be inadequate to take off the market all the commodities and services which our economy can produce at full employment, the federal government must step in to underwrite aggregate demand and

guarantee full employment By making public expenditures well in excess of the amounts which it subtracts from the incomes of the people, or by other methods, it must keep aggregate demand at such a level that there will be continued full employment for labor and other productive resources

If this desire for full-fledged underwriting of aggregate demand and guarantee of employment by the government is to be met, will it be possible for the government to make heavy expenditures in the process of creating employment without encroaching on the fields which are traditionally reserved for private enterprise? Some advocates of full-employment policy seem to have no worries on this score The necessary spending by the government, it is said, would go on in such fields as education, public health facilities, nutrition, slum clearance and housing construction, and resource development (projects like the Tennessee Valley Authority), where the need for public outlay is great quite apart from the question of full employment and where there would be little competition with private enterprise

However, the need for expenditures in these fields is not unlimited, and governmental spending for full employment might have to amount to 10 or 15 billions of dollars in some years, or even year after year if, as some people think, there is to be a chronic shortage of private spending for consumption and investment in our so called mature economy In such a case it would seem that the government might have to fall back on the multiplication of post offices and courthouses, if not on leaf-raking and hole-digging and refilling, if governmental spending were not to interfere directly with private enterprise On the other hand, if governmental policy in providing employment did involve direct competition with private enterprise, it might well discourage more employment-creating outlays than it furnished and lead to the gradual replacement of private enterprise by governmental enterprise

Even if it involved no direct competition with private enterprise by the government, the full-employment policy might still affect private enterprise adversely, for it might turn out to be a difficult policy for the government to administer successfully At best the policy would involve a fearful problem of estimation, and this problem would be complicated by the fact that private spending for consumption and the spending of private enterprises for investment cannot be taken as given entities to which we could simply

add governmental spending to provide employment In other words, the volume of spending by private individuals and firms for consumption and investment would almost certainly be affected by governmental spending for employment creation

Suppose, for example, that we are unwilling to increase the public debt any further, that we want the government to derive its funds for employment creation from taxation, and that large expenditures will be necessary Heavy taxes, even though levied progressively, will cut into spending as well as so-called unnecessary saving Individuals in the higher tax brackets may be rendered more unwilling than ever to put further capital funds into risky business ventures, since any gains that they make will be largely taken by the government while any losses which they suffer will be almost entirely their own Because of the necessity of paying heavy taxes, any capital funds actually seeking investment may be channeled largely into fields where the rate of return (net after taxes) promises to be high rather than other fields where it seems likely to be moderate or low This may produce distortion in the investment structure which will have unfavorable repercussions on employment in the end In view of such considerations, how could governmental leaders ever decide just how much additional tax revenue should be collected and spent in order to provide a given net increase in total employment?

If the governmental guarantee of full employment is to be carried out on the basis of deficit spending rather than taxation, the problem is no less complicated Heavy deficit spending may have an unfortunate effect on business confidence and arouse fears of higher taxes later on, with adverse effects on the amount of employment furnished by private industries and businesses Some prices may be more responsive than others to increases in the total volume of spending, and deficit spending may therefore cause changes in the relationships which prevail between the prices of different economic goods Such distortions of the price structure may then have a reflex influence on the volume of private spending and employment creation Again, deficit spending, besides providing employment, may raise the general level of prices, and there is no reliable way to determine in advance just how the influence of deficit spending will be divided between furnishing employment and raising prices However, it is likely that the latter influence will increase and the

former will decrease as the economy gets nearer and nearer to full employment

In the light of such considerations, and others which are sometimes mentioned, it would seem doubtful that any human wisdom would ever suffice to determine just how much deficit spending should be undertaken at any given time in order that a given number of people, who would otherwise be unemployed, may have employment. Presumably the deficit spending engaged in by the government in the 1930's was intended to induce recovery and achieve a high level of employment, and yet we know that unemployment continued on a large scale throughout the period. It is easy to look backward and decide that this spending was ineffective because it was carried out on too small a scale, but much more difficult to decide what scale of deficit spending would be adequate to ensure full employment a year or so in advance. High and low points in production and employment in our economy are easy to detect several years after they have occurred. It is quite another problem to determine them as of about the time when they occur, and practically impossible to determine them in advance, as would seem necessary if governmental expenditures for creating employment were to be based on an orderly, planned program.

It seems to follow that any estimates of governmental expenditures necessary to provide full employment, whether the program were to be based on taxation or deficit spending, would be likely to be wrong in practice. If the full employment scheme were tried over a period of years, the estimates of necessary governmental expenditures were always wrong, and chronic unemployment still troubled us, what would be the result? The program might be abandoned as impractical, but we may doubt whether the government would want to give it up and whether it would be allowed to do so. The government might confess its inability to provide full employment in our type of economic system and adopt the objective of maintaining merely as high a level of employment as possible. However, a half-hearted governmental program would not be likely to produce as high a level of employment as our economy could furnish in the absence of a governmental employment policy.

The government might decide to employ a "shotgun" policy, figuring that extremely large deficits, such as those that existed during World War II, could hardly fail to provide full employment. However, it may be questioned whether the government's credit in

a capitalistic economy and in peacetime could long sustain deficits of 50 billion dollars per year, and in any case the policy would be likely to produce a runaway inflation as well as, or instead of, full employment. The most likely notion of all is that the governmental leaders would decide that full employment could be maintained only if the government had the power to plan production, employment, wages, prices, domestic trade, external trade, finance, and virtually everything else, for the economic system as a whole. If these powers were granted, the planned and controlled economy would be at hand. No one doubts that full employment can be maintained in such a planned economy, but there is grave doubt that the government can control just employment and nothing else in a capitalistic system.

*Social Insurance under Capitalism* Another important phase of the status of labor has to do with the risks which workers bear and the extent to which these risks are provided for by a system of social insurance. Capitalistic countries in general now have such systems of social insurance and the United States is no exception to the general rule. However, the United States lagged well behind other countries in adopting a system of social insurance, and the benefits provided by our present system, for workers who suffer losses as the result of the risks which they must face, are none too generous. Forty-seven of the states have laws which require employers to provide in advance for the compensation of workers who become unable to work because they have suffered industrial injuries. Most of the laws exclude farm labor, domestic employees, itinerant or casual workers, workers in interstate commerce, and other specific types of workers. On the whole, about 80 per cent of all the workers are probably covered by the various compensation laws. Benefits to injured workers usually consist of a certain percentage of the workers' regular weekly wage, and they vary greatly from state to state. Maximum weekly benefits (prescribed by law) range from \$12 to \$25, and the number of weekly payments to be obtained by the workers depends on the nature of their injuries. Most of the laws set maximum monetary awards for cases of total or partial disability and only twenty states provide compensation which continues for life in cases of total disability.<sup>6</sup>

<sup>6</sup> P. T. Gemmill and R. H. Blodgett, *Economics Principles and Problems*, pp. 481-483.

Insurance against unemployment in the United States was provided for by the Social Security Act of 1935, which requires employers to pay a 3-per-cent tax on payrolls for this purpose. The federal government does not actually provide the unemployment insurance, but it encourages the states to do so, by permitting employers to credit as an offset against the federal payroll tax any amounts (up to nine tenths of the federal tax) which they contribute to any approved state funds for unemployment insurance. All the states had adopted unemployment insurance systems by July, 1937, but the unemployment insurance which is provided is far from adequate. The Social Security Act failed to provide for workers who are employed in enterprises which do not have a labor force of at least eight workers for at least twenty days a year (each day being in a different calendar week). It also excludes workers employed by relatives, agricultural workers, employees of nonprofit-making institutions, public employees, offices and crews engaged in shipping in United States waters, and domestic servants in private homes. On the whole, about two thirds of the "gainfully employed" workers are covered by unemployment insurance.

The benefits provided for unemployed workers vary greatly from one state plan to another. The maximum weekly benefit payment was \$15 in most states before the war, but was \$16 to \$18 in a few. The minimum weekly payment, where specified, ran from \$1.50 to \$10. The weekly benefits actually paid to completely unemployed workers in 1940 ranged from \$4.68 to \$14.14, with an average of \$10.57 for the whole country. The annual benefits ranged from \$42.60 to \$174.12, with an average of \$100.15 for the whole country. The state plans usually require workers to be unemployed for two or three weeks before beginning to receive benefit payments and usually provide that no worker can receive more than sixteen weekly benefit payments in any one year. Some states raised their maximum benefit payment during World War II, and it is now as high as \$22 in a few states. In 1946, the average amount of benefit was \$18.50 a week and the average period of benefit payments was 13.4 weeks.<sup>7</sup> It is scarcely necessary to say that the unemployment insurance system is inadequate, though it is admittedly better than having no system at all.

The Social Security Act of 1935 (as amended in 1939) also provides for a system of annuities for workers over sixty-five years of

<sup>7</sup> *Ibid.*, pp. 471-472.

age who have contributed regularly to the building up of a fund for this purpose Both employers and employees contribute to the fund by means of tax payments, which amounted to 1 per cent of the first \$3000 of wages or salaries from 1937 through 1947. The contributions are to increase eventually until they amount to 3 per cent each for employer and employee, or a total of 6 per cent of the taxable portion of each eligible employee's compensation About the same classes of workers are excluded from the annuity scheme as from the unemployment insurance plans.

The annuity payments will vary according to the size of each worker's wage during his years of employment and the number of years through which he and his employer have contributed to the fund In general, as figured by a rather complicated method, they will range from \$10 to \$85 per month This means that, if the contributions are made on the maximum eligible wage or salary for the maximum period of time, the annuity will reach \$1020 per year, or roughly one-third of the maximum eligible wage or salary Under the 1939 amendment of the Social Security Act, supplementary payments may also be made to certain dependents of retired workers, but the law limits the total annuity going to a retired worker and his family each month to twice the amount of his primary benefit (his own annuity), or 80 per cent of the worker's former average monthly wage, or \$85 per month, whichever is the least The 1939 amendment also provided for benefits to certain survivors of the retired workers For example, a wife who survives her husband and is over 65 years of age receives three-fourths of his former primary benefit At the end of 1946, the average monthly benefit paid to retired workers was \$24 60, to wives of retired workers, \$13 00, to children, \$12 55, to aged widows, \$20 20, to widows with a child or children \$20 10, and to dependent parents, \$13 15<sup>8</sup>

On the whole, the opinion is widespread that our system of social insurance leaves much to be desired and, for some years now, the air has been full of proposals for extending it Such extensions might take any or all of three forms An effort might be made to bring into the social insurance system those groups of workers who are now excluded, overcoming in some fashion or other the administrative and other difficulties which would be encountered The types of insurance might be extended to cover illness, medical expenses, hospitalization, and the costs of maternity And the benefits might

<sup>8</sup> *Ibid*, pp 496-497

be enlarged and made to run for a longer period of time than at present. For example, there is a proposal that the maximum benefits for full-time unemployment should be made not less than \$25 a week and that benefits should be payable for a total of at least twenty-six weeks in a year.

There is little doubt that the social insurance system should be extended, but the question of just how far is still a lively one, for some people have a definite conviction that an overextension of social insurance would do more harm than good. Insurance against practically all the eventualities covered by social insurance can be obtained from private insurance companies, but it is objected by virtually everyone that the workers cannot afford such insurance. How then can they afford insurance against the same risks through a governmental system? Unless one is willing to make the probably ridiculous assumption that the government can operate insurance projects more cheaply and efficiently than private companies can, the answer is that the workers cannot afford it if they have to pay all the costs of protection and benefits which they receive. If the social insurance system is to be of much benefit to the workers, they must be allowed to take out more than they put in, with the balance of the funds coming from general governmental revenues, contributions of people other than the workers themselves, or other sources. From this point of view, social insurance is a device for redistributing the income of the country—a means of taking from some and giving to others—and there is a question of how far this process can or should be carried in a capitalistic system.

It is also possible that an overextension of social security might have unfortunate effects on the beneficiaries themselves. Too much insecurity may be a bad thing for the workers, but a little insecurity may not be. Under a complete system of social security, troublesome problems of absenteeism, lateness to work, undue labor turnover, and soldiering on the job might arise. And there is also the problem of malingering. It would surely be unfortunate to encourage people to take two or three months off to get over a cold or to work only half of each year while retaining on unemployment benefits during the other half. It is probable that there are millions of people in the country today who would prefer a moderate income, with no work attached, to a somewhat larger income with full-time employment.

Attempts to solve such problems under a complete system of

social security might well involve severe governmental restrictions on individual freedom. We cannot intelligently set out to make people well off regardless of how they behave. We can follow through on our intention to make them well off only if they behave in certain ways. If they will not behave in these ways voluntarily, then it will probably be necessary to make them do so. Of course, the advocates of social security do not put the matter in this fashion. They say that it may be necessary for the government to give the individual citizens a little friendly advice and supervision. In all probability, however, under too great an extension of social security, we would learn the truth of the proposition which says that, if the government assumes responsibility for the individual's welfare, it must also take control of the individual's conduct.

### *The Status of Labor under Socialism*

***Wages, Hours, and Working Conditions*** The status of labor under ideal socialism would be quite different from that which it has under capitalism and according to socialists it would be a greatly improved status. With the government operating most industries, most of the gainfully employed would be governmental employees and, with the land and capital of the system owned for the most part by the people as a whole through the government, the citizens would receive practically all their money income in the form of wages. Since the government under ideal socialism would be merely an agency representing or operating in the name of the people as a whole, the workers of the system would really be working for themselves and they could expect to share, through their wages, almost the entire national real income which was available for consumption.

A socialistic economy would necessarily be a planned economy and the economic plans of the system would have to include the total amount to be paid out as wages. In similar fashion, the wage rates to be paid for various types of labor would have to be determined by planning, either specifically or within rather narrow limits. Differences in wages as between industries and occupations would certainly prevail, both to reward the various workers for their differential accomplishments in production and to secure a distribution of workers among industries and occupations which would be consistent with the carrying out of the economic plans of the system.

for a socialistic economy would hesitate to attempt to distribute or allocate workers arbitrarily among industries and occupations. However, the differences in wages and salaries under socialism would be very small in comparison with those which traditionally prevail under capitalism, because the values of the workers' products and hence of their productive services would be determined not by the economic forces of a free market but by the planners' notions as to the social value of these products and services, and because all persons would have an opportunity to acquire the education and training necessary to the breaking down of the environmental barriers to eligibility for the better paying jobs.

In so far as a socialistic system would depend upon wages to furnish incentives or motivation for the workers, it would be expected that some type of incentive wage system would be used to reward the workers for turning out greater quantities and better qualities of product. However, such a wage system would be protected from the worst abuses which it might contain under capitalism. Minimum hourly or daily wages would probably be set up and these would be paid to all workers employed in a particular type of work, with the incentive differentials superimposed on these minimum wages. Moreover, the incentive wage system would not be used as a device for speeding up and then exploiting the workers. That is, after the incentive differentials had induced the workers to increase their output, there would be no profit-seeking capitalistic employers to cut piece rates so that the workers would have to work much harder than formerly to obtain even their former earnings. On the other hand, as we noted in the preceding chapter, a socialistic system would not depend entirely on differences in earnings to furnish incentives to the workers. Many other economic and non-economic incentives would be employed to spur the workers on to high productivity and accomplishments.

We cannot conclude in an offhand fashion that real wages would be higher in a socialistic economy than in a capitalistic economy. The level of real wages under socialism would depend on many factors, such as (1) the quantity and quality of land and natural resources available in the system in relation to the size of the population, (2) the presence or absence of large quantities of highly skilled and trained labor, (3) the effectiveness of the incentives of the system and the size of the total national income which resulted, (4) the skill with which the planners did their work and the smooth-

ness with which the plans were carried out, and (5) the temper of the planners and the way in which they divided the productive resources of the economy as between turning out goods for immediate consumption and the production of capital goods or armaments and equipment for war. Other things equal—that is, under any given conditions with respect to productive resources, labor supply, efficiency, size of the total national income, and division of the national income as between present and future needs—the great masses of workers under socialism should be better off than under capitalism because of the much more equal division of the consumable portion of the national income. On the other hand, managers and officials of enterprises would not be able to command the large incomes which go to them under capitalism.

The crux of the whole matter, from the point of view of the workers, would be the absence, under socialistic democracy, of any large class of persons who could feather their own nests by mistreating the workers. With no profit-seeking enterprises in a position to make larger profits by holding down wages, it would be expected that wages would absorb almost the entire consumable portion of the national income. Since there would be no one to gain by employing the workers long hours under miserable working conditions, it would be expected that hours and working conditions would be as favorable as they could be and still be consistent with the economic plans of the system. On the other hand, if the government were not democratic under socialism, it might be possible for the ruling bureaucracy to secure itself firmly in power and replace the capitalistic enterprises as a class which could profit by holding down wages and insisting on long hours of labor under unfavorable working conditions.

*Labor Organizations under Socialism.* According to the prospectus, labor organizations or unions would be not merely tolerated but actively encouraged under socialism. The labor unions would presumably be of the industrial rather than the craft type, so that they would represent the great industrial group interests rather than the narrow stratifications of labor. The functions of labor unions under socialism would differ considerably from those which they have under capitalism. In the first place, the unions would not be bargaining and fighting organizations primarily under socialism. Since the workers would receive virtually the entire consumable portion of the national income as wages, there would be no other

large classes of income receivers to fight with over matters of income distribution, and there would be very little to fight over since the various workers would share rather equally in the consumable portion of the national income. Collective bargaining would still exist between labor unions and management, but only to determine the exact wage rates, hours and working conditions, within the rather narrow limits set by the economic planners, which should prevail in particular plants and industries. Collective agreements, embodying the exact terms agreed upon, would probably be drawn up for specified periods of time.

Labor unions under socialism probably would not be allowed to use strikes, boycotts, and other customary weapons of organized labor under capitalism. Since the workers as citizens would be part owners of the various industries of the economy, the workers of any particular industry could only strike against themselves or against other groups of workers, and neither procedure would be very sensible or profitable. The workers of any one industry would know that demands for higher wages on their part would be met by similar demands by the workers of other industries and that the workers as a whole cannot obtain as wages more than the entire consumable portion of the national income regardless of what might happen to wage rates or the sum total of money wages paid out. Moreover, it is planned that the workers under socialism will be represented, through their unions, in the management of all sorts of enterprises and industries. This in itself would have the effect of moderating the demands of the workers since they would be more conscious than usual of the problems of management and would no longer merely be familiar with their own side of the picture. Being represented in management, labor unions could place their legitimate claims before the responsible officials without any show or use of force. Since it has been so steadfastly denied them under capitalism, this privilege of being represented in the management of industries and enterprises should mean a great deal to the workers.

Besides the bargaining and managing functions, labor unions would carry on many types of activities under socialism. Individual grievances between workers and management would still arise in the best regulated economy, and the unions would play an important part in the settlement of such cases. When individual workers complained that they were not receiving the wages to which they were entitled, that they were being made to work unduly long hours, that

their advancement was being retarded for personal reasons, or that they were being discriminated against in other ways, the unions would step in and help iron out the difficulties. The unions might well be entrusted with the management of the various social insurance schemes and funds which the economy would operate. They would probably be expected to cooperate with management in handling problems of labor absenteeism, lateness to work, and undue labor turnover, and in stimulating the workers to increased efficiency and productivity. Finally, the unions would carry on a variety of cultural, social, educational, and recreational activities, as they do under capitalism.

*Social Insurance under Socialism* An ideal socialistic system would undoubtedly have a complete and adequate system of social insurance to provide economic security for the workers. Indeed, socialists claim that a really comprehensive scheme of social insurance can be efficiently operated only in their system. Under socialism, all the risks of the workers would be pooled, the various types of benefits would be closely integrated with each other, wages, contributions, and benefits would be properly coordinated in connection with each type of social insurance, and the cost of the insurance would be placed immediately and directly where it belongs—that is, on society as a whole. Of course, the details of the various social insurance plans cannot be predicted accurately in advance. However, the socialists contend that there would be no need for unemployment insurance in their economic system, and all other social insurance schemes would be supplementary to their requirement that all able-bodied persons should work if they wish to receive income and to their proposal for incentive wage and salary systems.

*Employment under Socialism* The socialists contend that there would always be employment for all available labor in their system, for the chief cause of unemployment under capitalism—business depressions—could be eliminated. Society as a whole, operating through the government, would be the only business enterpriser of importance, the results desired from economic activity as a whole would be planned before the individual phases of this activity were undertaken, competitive wastes would be eliminated, and the conflict of individual and social interests would be a thing of the past. As productive activities expanded, there would be no private enterprises to fear the future and strive to protect profits or minimize

losses, and society as a whole, as we have suggested on previous occasions, is and should be tremendously indifferent to money profits or losses. This is not to say that business cycles would be automatically eliminated under socialism, for their elimination would depend upon the skill with which the economic system was operated. However, such a system should be able to prevent cyclical fluctuations if an earnest effort was made to secure this result, for under socialism there never would come a time in the expansion of productive and distributive activities when it would become necessary or desirable for society, as the only enterpriser, to retrench, cut production, discharge workers, curtail the purchase of materials and supplies, and so on, because of considerations of money profit and loss. With production based on and adapted to social needs, there would be virtually no fear of business cycles because there are no cyclical fluctuations in social needs for economic goods which could produce cyclical fluctuations in economic activities. Under such a system, production in individual lines would be curtailed only when goods of certain kinds were being produced in sufficient abundance for the satisfaction of human wants.

Under these conditions, say the socialists, only incredible stupidity would permit any significant volume of unemployment to exist for workers or for other productive resources. Since society as a whole, as the enterpriser, would not have to make profits from the employment of workers and other productive agents, it would not be difficult to find things for all the productive agents to produce. Agents of production would be regarded as "profitably employed" from the social point of view as long as they produced things which the members of society needed or desired, a concept which would furnish virtually limitless possibilities for employment in view of what is known about the nature of human wants. Of course, socialists hope and expect that technological changes and improvements would continue to be made in their system, and it would be inevitable that such innovations would displace workers at times, but it should be possible for a socialistic system to hold such displacements to a minimum. Some industries would still show a degree of seasonableness in their labor requirements under socialism, but in other cases the seasonableness which exists under capitalism could be reduced greatly, if not eliminated. In any case, if workers were thrown out of employment for any reason under socialism, they would have excellent prospects of being reemployed if the

economy maintained the policy of affording employment for labor as long as labor could produce goods which the citizens needed or desired

**Population under Socialism** A socialistic economy might conceivably adopt a population policy as a temporary expedient, but no definite policy in this matter is in prospect for such an economy. On the whole, it would seem that conditions would be favorable for an increasing population under socialism. In fact, some critics of socialism contend that the population of such an economy might increase so rapidly as to constitute a problem. The theory is that population growth is held in check under capitalism by the desire of the citizens for economic advancement and a high standard of living, since an oversupply of children may keep a family from getting ahead. Under socialism, with employment at good wages guaranteed to all and support assured for one's children as well as for oneself, the size of families might increase so rapidly as to bring about a sharp reduction in standards of living despite the best productive efforts of the citizens. These arguments are, of course, in the field of speculation. The number of children which a family will contain is influenced, in any system, by a large number of considerations or forces many of which are noneconomic in character. The pressure of public opinion might go far toward preventing an unduly great increase in numbers. Moreover, under capitalism, the largest families are often found in the most wretched and miserable groups of citizens, and there is no certainty at all that a general improvement in living standards would lead to an unduly rapid rate of population growth under socialism.

**Labor under Communism** In most of these matters which are connected with the status of labor, there is little reason to think that conditions under ideal communism would differ greatly from those of ideal socialism. Of course, workers would be expected to distribute themselves among occupations and industries on the basis of their ability to contribute to the welfare of society and not on the basis of differentials in wages. They would be expected to work according to their ability, and in return they would receive real income and consume on the basis of their needs. Otherwise, a communistic system would probably offer, at least in theory, the socialist goals of full employment, satisfactory hours of labor and working conditions, social security, and the right of labor to organization.

*The Status of Labor in Soviet Russia*

Before the outbreak of war with Germany, there were some 30.4 million workers in what the leaders of Soviet Russia call the "national economy."<sup>9</sup> Of this total, between 11 and 12 million were in industry, over 3 million were in various branches of transportation, some 2.5 million were in trade, almost 2 million were in construction, and about 3 million were in agriculture. Agricultural workers in the national economy included only those employees who worked for wages and not the collective farmers or individual peasants. During World War II, the number of workers in the national economy declined to 27.3 millions, but it had recovered to 30.3 millions by the end of 1946. The goal for 1950 is 33.5 million workers.<sup>10</sup>

*Wages, Hours, and Working Conditions.* The Russian workers find the basic specifications, or maximum and minimum requirements, concerning their wages, hours, and working conditions in the Labor Code of 1922, as amended by several later decrees. The standard work day for industrial workers and office employees, prior to June, 1940, was seven hours. A six-hour day was standard in various difficult and dangerous occupations and for young workers between the ages of 16 and 18. Except for purposes of training, no employment was permitted for persons under 16 years of age. The work week was continuous, and productive facilities were operated by means of three shifts per day, but the individual workers enjoyed a day off after every five days of work. Thus, while rest days were frequent, there was no definite day of rest for all the workers. The workers were entitled to an annual vacation of from two weeks to a month with full pay. It is hardly necessary to say that these conditions compared very favorably with those which prevailed in the leading capitalistic countries.

Most of these conditions were changed for the worse during the period of World War II. In June, 1940, the standard work day was increased to eight hours for ordinary workers, and to seven hours for very heavy work, though the six-hour day was retained for exceptionally dangerous or harmful work. Eight hours also became the standard day for office workers and for young workers between the ages of 16 and 18. The continuous work week for productive facilities and the five day work week for individual workers were elimi-

<sup>9</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 70.

<sup>10</sup> *Ibid.*, p. 71.

nated. The common six-day work week was instituted and the seventh day, Sunday, became the day of rest for workers in general. The Ministries were given the power to extend or abrogate the collective agreements which were then in force. In July, 1941, a decree made it possible to require two or three hours of overtime work per day, with pay at the rate of time and one-half for the overtime. All vacations for workers were discontinued, but additional compensation was provided for work during what would normally have been vacation periods.<sup>11</sup> These changes were comparable to those which occurred in other countries under wartime conditions. By 1948, the wartime practice of general overtime work had been eliminated, but the eight-hour day had been officially substituted for the seven-hour day as the basic work day for peacetime conditions. It is probable that this eight-hour day and the 48-hour work week will be continued for some time.<sup>12</sup>

As previously suggested, general conditions with respect to wages are established by the Labor Code and the supplementary decrees, while the total funds to be used for wage payments annually in individual industries and in the economy as a whole are determined by the economic planners. Then specific levels of wages and wage differentials are established for the various industries by the Council of Ministers, the individual ministries, and ostensibly by collective bargaining between labor unions and management. In practice, however, collective bargaining resulting in collective agreements was widely abandoned after 1934 and was revived again only in 1947. The subjects to be covered by the new collective agreements are increasing the productivity of the workers, the substitution of piece rates for time rates and the improvement of production norms, programs for training workers and technical personnel, devices for improving labor discipline, measures to improve the safety of working conditions, the improvement of the workers' housing, living conditions, and food, and the improvement of recreational facilities for workers.<sup>13</sup>

Wages are on a piecework basis in Soviet Russia wherever possible and are intended to give due regard for the skill required. Even before the war, about three-fourths of all wages were based on piece

<sup>11</sup> These changes were reported in the *American Review on the Soviet Union*, April and June, 1941, *Foreign Commerce Weekly*, March 8, 1941, and *International Reference Service*, May, 1941.

<sup>12</sup> Harry Schwartz, *Russia's Postwar Economy*, p. 76.

<sup>13</sup> *Ibid.*, pp. 78-79.

rates and in about a third of the cases provided additional bonuses or premiums for increased quantities or improved quality of output. We have commented already on the extent of differentials in wages or earnings in the preceding chapters and need only say here that these differentials are intended to be adequate to give incentives to all classes of workers, though the Soviet system does not intend to depend altogether on such economic incentives. In general, the piecework system of wage payments is allowed to operate as a genuine incentive wage system, for production norms are raised or piece rates cut only in emergency situations or when the old norms or rates have become clearly outmoded.

Still other economic rewards, as well as honors, are available for exceptional workers in Russia. Unusually efficient workers may be given the title of Heroes of Socialist Toil, which carries with it extra pay of from 10 to 50 rubles per month, exemption from certain taxes, reduced rent, free street car service, increased social security benefits, and protection from summary eviction from living quarters. The government was active in encouraging the Stakhanovite movement, which led to large increases in the productivity and earnings of many workers. Many purely honorary awards are also used, as we have seen previously. The liking of the workers for the system is supposed to be indicated by the enthusiasm with which they engage in socialist competition and undertake extra work without compensation on their free days.

The wages of Russian workers also suffered to some extent in the war and early postwar periods. After increases of 15 to 50 per cent in work quotas (norms for the incentive wage systems) had occurred beginning in 1936, after the Stakhanovite movement had indicated that the old quotas were greatly out of date, further changes were made in 1940. It was then decreed that work quotas should be increased and piece rates decreased in proportion to the increase of the working day which occurred at that time, and that existing rates of pay for workers paid by the day and monthly rates for salaried employees be retained in spite of increases in hours. The net results were both increased hours of work and reduced hourly rates of pay. Thus, the Russian government eventually came to treat the workers as it had often accused capitalistic employers of treating them.

Similar developments occurred in the early postwar period. In September, 1946, substantial increases in the prices of rationed foods

were made, with most of them rising to roughly three times their wartime levels, while wages were increased to a much smaller extent. Then in March and April, 1947, work quotas were raised again for workers on the piecework basis. Such increases in work quotas result in wage cuts for workers who do not increase their outputs, since workers are often paid both bonuses and higher piece rates for production in excess of their norms or work quotas. Higher norms therefore mean that workers must produce more before they can begin to cash in on the higher piece rates or bonuses.

*Criticisms of Russian Wages, Hours, and Working Conditions*

We noted in the preceding chapter that the Russians have attempted to use the piecework basis of wage payment for some types of work which in other countries would not be considered well suited for this system. In some cases, the piecework system has led to the turning out of large quantities of low-quality product, to an unduly large amount of overtime work, and to a failure to use safeguards for workers in cases where such devices would lower the speed at which work could be carried on. The Stakhanovite movement led to great increases in productivity in many cases and made possible a revision of obsolete production standards, but it had many bad effects. It led to a craze for record-breaking, and many a spurious record was set up by especially selected workers under artificially favorable conditions. Elementary rules for the safety of the workers were forgotten, accidents increased in number, and the health of the workers suffered. Machinery and equipment were carelessly used and large quantities of spoiled and incomplete products were turned out. The raising of production standards aroused discontent among the masses of ordinary workers who were not capable of achieving records, and the high earnings of the Stakhanovists put them in a social class by themselves. Finally, some writers hold that the movement concentrated attention on increasing productivity by means of an intensification of effort on the part of individual workers to the neglect of the important factors of scientific management and organization of production, which also greatly needed improvement in the Russian system. It is only fair to say, however, that other writers hold exactly the opposite opinion on this last point.<sup>14</sup>

The more determined critics of the Russian system profess to regard it as a dictatorship over the proletariat rather than a dictatorial

<sup>14</sup> See A. Yugow, *Russia's Economic Front for War and Peace*, pp. 190-195, and A. Bykov, *The Development of the Soviet Economic System*, pp. 336-337.

ship of the proletariat and contend that the wages, hours, and working conditions specified by the laws and collective agreements are meaningless except as a device for deceiving outside observers of the Soviet system. In practice, it is said, the managers of Russian enterprises are under great pressure to fulfill the plans and are subject to severe punishment if they fail to do so. As the lesser of two evils, they rather openly violate the conditions of the Labor Code. Workers are compelled to put in 14 or 16 hours per day rather than 8, and 9 or 10 hours, instead of 7, in the heavy or dangerous occupations. They are also compelled to work on their so called rest days. While the workers are said to "volunteer" for such extra work, it is actually proposed to the workers by Party men, and workers who do not volunteer are turned over to the NKVD as counter-revolutionaries. Occasionally, labor grievances are investigated, blame is placed on certain managers, union officials, or Party men, and a few offenders are liquidated, whereupon the system continues operating as before.<sup>15</sup>

Certainly it is true that, in the past few years, the Soviet Russian system, made desperate by problems of labor turnover, absenteeism, and lateness to work, imposed very severe controls on the individual workers. Starting in 1938, each worker was made to carry a labor book which contained a full record of his career, including social origin, history, training, types of employment, past sins and fines, and reasons for dismissal from past jobs, or for changing jobs without being dismissed. A worker could not be hired unless he had this labor book and workers with unfavorable records sometimes had difficulty in getting jobs. During the war period, many new workers did not have labor books and managers were allowed to disregard this matter in hiring workers. However, the old system was reestablished in the fall of 1946.

Also beginning in 1938 a worker had to give one month's notice in order to give up his job even when he was not under contract, and a worker who left without notice or was discharged for crimes or breaches of labor discipline could be evicted summarily from his living quarters and denied such quarters elsewhere. One day's unjustified absence from work might bring dismissal and eviction, while any malicious breach of labor discipline might mean dismissal and criminal prosecution. Any worker who was late to work without sufficient reasons, left early for lunch, returned late from

<sup>15</sup> F. Utley, *The Dream We Lost*, pp. 172-178.

lunch, left the enterprise early, or loafed in working time, was considered guilty of a serious offense. Three such violations in one month, or four in two consecutive months, could result in dismissal. Vacations were granted only to workers who had been employed at least eleven consecutive months in one job, and workers who had spent more than two years in a single position were granted longer vacations and increased social security benefits of one kind and another.

Under wartime conditions, further regulations were issued which bound the workers firmly to the enterprises which employed them. Workers could leave their jobs only if the managers of the enterprises gave their permission, and such permission could be given only in cases of incapacitating illness, invalidism, or assignment to study. Workers who gave up their jobs without permission could be punished by imprisonment for two to four months. Even absence from work could be punished by six months of correctional labor at the usual place of employment at a 25-per-cent reduction in wages. On the other hand, after October, 1940, each Ministry had the power to transfer engineers, construction workers, foremen, draughtsmen, bookkeepers, economists, financial and planning workers, and other skilled workers from one plant to another, regardless of location. However, such workers kept their seniority rights, received credit for their experience, and were allowed to take their families with them. They received transportation allowances, wages during their trips and for six days after, and a subsidy equal to three or four months' wages to help them to get settled.<sup>16</sup>

Before 1940, these restrictions on labor and severe penalties for breaches of labor discipline had no very important practical effects, perhaps because then strict enforcement would have deprived many Russian enterprises of their labor supply. In June, 1940, however, plant managers and heads of governmental bureaus who fail to prosecute workers guilty of breaches of labor discipline, or who hire workers who are hiding from prosecution as a result of breaches of labor discipline at other plants or bureaus, were themselves made liable to prosecution and imprisonment for three years or less for abuse of power or nonexercise of power. Some plant managers have been removed from their positions and sent to prison under this decree, and so have doctors who have shown a "lack of class consciousness in the issuance of hospital certificates," and public prose-

<sup>16</sup> *American Review on the Soviet Union*, April, 1941.

cutors and judges who have failed to prosecute or punish workers or managers under the various decrees

*Real Wages and Standards of Living* Even if we were to take the Labor Code and subsequent decrees at their face value with respect to the wages, hours, and working conditions of Russian labor, we should have to remember that real wages must depend ultimately on the total productivity of the Russian economy As long as this productivity remains low and the national real income available for consumption remains small, the system of wage payments may be very fair and the hours and working conditions very favorable, and yet the Russian workers will not be well off with respect to real wages and standards of living By all accounts, therefore, the real wages and standards of living of the Russian workers remain low by comparison with those of the workers of the leading capitalistic countries Just how low they are is difficult to determine because of special peculiarities of the Russian situation.

In summarizing the difficulties of estimation, one writer says

The greater part of the income of the agricultural population is in kind No study whatever has been made of the social stratification of either town or country The needs of the population have greatly increased since the Revolution and have undergone substantial changes in the kind of goods in demand The published wage rates are merely the minimum rates established by law and only averages are published There are no official indexes or family budgets to serve as a basis for estimating real wages There is no regular official publication of the prices of the basic articles of consumption Until 1935 workers were paid partly in money and partly in kind Prices for the same articles in government, kolkhoz, and private stores differed widely No studies have been made of fluctuations in the purchasing power of the ruble Such studies of the budgets of workers or kolkhoz members as have been made relate to small groups of those most favorably situated<sup>17</sup>

Sometimes an attempt is made to get at the standards of living of the Russian workers by calculating that the ordinary worker would have to use four months' wages to purchase a pair of shoes or a suit of fair quality, and a week's pay for a shirt, and so on This approach is not very helpful, for we do not know that such articles are as important in the standards of living of Russian workers as in those of our own workers, or even that the articles, though familiar enough to us, are really a part of that quantum of commodities and

<sup>17</sup> A Yugow, *Russia's Economic Front for War and Peace*, p. 198 Reprinted by permission of the publishers

services which ordinary Russian workers feel that they must have. However, it is possible to say that, at the end of the Second Five Year Plan, the average annual per capita consumption of meat in Russia was 211 kilograms, as compared with 62 kilograms in the United States and England, and 48 kilograms in Germany. Per capita milk consumption in Russia was 170 kilograms, as compared with 400 kilograms in England and 355 in Germany. Sugar consumption in Russia was about  $1\frac{1}{2}$  times greater than in pre-Soviet days, but it remained only half that of Germany, two-fifths that of the United States, and one-third that of England.<sup>18</sup>

Studies of consumption among the workers in large-scale industries in Moscow, Leningrad, Kharkov, and other large cities indicated that in 1937 the average worker had 0.9 of a suit of clothes and 1.5 pairs of shoes. Some 20 per cent of the workers' families had radios, 3 per cent had phonographs, 2.8 per cent had bicycles, and 0.8 per cent had cameras.<sup>19</sup> These conditions in consumption were what we should expect on the basis of what we have learned concerning the heavy rate of capital accumulation and investment in Russia, the underfulfillment of plans for the production of consumers' goods, and the rationing of many products. On the other hand, there was no doubt that the standards of living of the Russian workers were improving, though slowly, in the years before World War II.

During the war, the standard of living of the average Russian workers received a sharp setback, for the production of consumers' goods at the worst fell to about half the 1940 level. A considerable recovery occurred soon after the war, but it was not until late 1947 that production in general reached the level of 1940. This left the Russian workers as consumers very badly off, because the production of consumers' goods showed the usual tendency to lag behind production in general, and the attainment of the 1940 level of consumers' goods production, had it occurred, would not have brought the consumers back to 1940 levels on a per capita basis because of population changes. In the years to come, we may expect real wages and standards of living of the Russian workers to improve beyond the 1940 level, in the absence of further wars. Moreover, if the real income of the Russian economy ever becomes as great in proportion to population as that of the United States, we may expect the ordi-

<sup>18</sup> *Ibid.*, p. 203.

<sup>19</sup> *Ibid.*, p. 212.

may Russian worker to be better off than the ordinary American worker with respect to living standards because of the more equal division of income which exists in Russia.

*Labor Unions in Russia.* Russian workers are not only permitted but also encouraged to belong to labor unions, and practically all of them do so. The unions are organized on a national industrial basis for the most part, rather than on a craft or establishment basis. That is, a union is likely to include all workers throughout the country who work in enterprises turning out the same kind of product. The Russian labor movement is thoroughly organized all the way from local and factory committees through inter-union district or city councils and regional or republic councils to the All-Union Congress of Trade Unions and the All-Union Central Committee of Trade Unions. The union members pay dues which amount to about 1 per cent of their wages.

The functions of Russian labor unions are quite numerous, at least in theory. In the first place, they are supposed to bargain collectively with management concerning the exact wages, hours, and working conditions which are to prevail in individual industries and occupations. Secondly, they are supposed to participate in the work of management. This involves discussing, and advising management with respect to, the economic plans for particular industries and helping to make actual managerial decisions. It will be remembered that the important managerial decisions in each plant or enterprise were originally to be made by a triumvirate, or Troika, composed of the manager of the enterprise, a Party representative, and a union representative. Thirdly, the unions cooperate with management in several respects. They promote labor discipline (by discouraging absenteeism, lateness to work, and labor turnover), encourage socialist competition, try to improve the worker's skill and increase productivity, take some responsibility for the maintenance of machinery and equipment, handle the minor delinquencies of union members, engage in labor recruiting, and in general work for the fulfillment and overfulfillment of the plans. Finally, the unions carry on several functions for the benefit of their members. They protect workers against accidents by promoting and enforcing safety measures, see to it that healthful and pleasant working conditions are maintained, carry on factory inspection, administer social insurance and relief systems, protect the workers against arbitrary

treatment by management, and carry on a variety of activities in connection with vacations, education, recreation, and culture.

All this gives us a rather favorable picture of the status of labor unions in Russia, but the critics of the system, while they do not deny the widespread membership of the unions, contend that their alleged functions are a sham and a delusion. The collective bargaining function amounts to nothing at all, it is said, because wages, hours, and working conditions are strictly determined by state agencies and the unions never question them. In fact, they do not even bother to insist on collective agreements in many cases. Union participation in management is purely nominal. All members of the Troika were likely to be Party members in the old days, which meant that their decisions would be in line with Party objectives. If any member of the Troika was not a Party member, it was likely to be the trade union representative, which meant that he would be powerless in comparison with the other members. Thus, the union representative would content himself with recommending the installation of drinking fountains or shower baths and would avoid questions of great importance to the workers. In any case, the Troika was abolished in 1937, and each manager was placed in full charge of his plant. The unions are said to be completely unable to protect the workers against summary dismissal, eviction, or imprisonment, against violation of the wages, hours, and working conditions provided by law, or against the violation of safety codes and other protective measures. Then "cooperation with management" means merely that they function as slave-drivers, employment bureaus, and collectors of forced loans. They represent the interests of the ruling bureaucracy and not those of the workers. According to this opinion, real labor unions do not exist in Russia today any more than they did in Nazi Germany.<sup>20</sup>

*Social Insurance in Russia.* Soviet Russia has a rather comprehensive system<sup>21</sup> of social insurance. According to the official version, there is no unemployment in the Soviet economy, and no unemployment insurance is necessary, but benefits are provided in connection with illness, accidents, old age, death, and childbirth. Benefits for workers who become ill begin at once and amount to full wages for workers receiving up to 180 rubles per month, in addition to free medical attention. The benefit for total disability may be as much as the full wages formerly earned, and in cases of partial disa-

<sup>20</sup> F. Utley, *The Dream We Lost*, p. 178.

bility a compensatory wage, equal to the difference between former and present earnings, is paid Death benefits include burial expenses, immediate financial assistance, and pensions for surviving dependents The pensions run from one-third of former wages for one dependent up to three-fourths of former wages for three or more dependents Old age benefits run from one third to 100 per cent of former wages depending on circumstances In general, an ordinary worker who has been employed for 25 years or more may expect to retire at age 60 on about 50 to 55 per cent of former wages The provisions for women workers and workers in dangerous trades are somewhat more favorable Women receive maternity benefits, and maternity leave consisting of eight weeks before and eight weeks after childbirth All expenses of social security are paid by management and added to cost The expenses for various enterprises and types of workers run from 10 to 20 per cent of the wage bill and average some 14 per cent Admission to benefits and the actual distribution of funds are in the hands of the labor unions Total expenditures for education, health service, social security, and other cultural purposes were supposed to reach 48 billion rubles in 1941 and are scheduled to hit 106 billion rubles in 1950

Criticisms of the Russian system of social insurance are fairly numerous Quite a large number of persons are excluded from the system (including members of nomadic tribes, peasants, hunters and fishers, and collective farmers) Comparatively few citizens have been able to receive the benefits up to the present time A few years ago only 125,000 persons out of 170,000,000 were receiving old age benefits Those who receive the benefits apparently do not get the full benefits provided by law in many cases When the cost of social insurance is borne rather directly by the general public, it is difficult to prevent malingering and other anti-social practices Workers who have been ill or injured pretend to be unable to resume work when in fact they could do so, and pregnant women hide themselves out as industrial employees in order to get the maternity benefits Finally, the social insurance benefits have been used to try to prevent labor turnover It is reported that full social insurance benefits are paid only to workers who have spent six years or more in one job

*Unemployment in Russia* The leaders of the economy proudly refer to Russia as the land without unemployment The federal constitution guarantees employment as one of the fundamental rights

of the citizens, and the planned economy has apparently gone far toward making good on this guarantee in practice. The First Five Year Plan predicted a considerable decline in the volume of unemployment and a reduction in the number of registered unemployed from 2,000,000 to 550,000. Actually, the unemployed were put to work much more rapidly than had been expected, and unemployment insurance and the labor exchanges were eliminated in 1930. Since then the official verdict has been that Russia has been struggling with a labor shortage rather than a problem of unemployment.

Critics of the Soviet regime, however, doubt very much that Russia should be considered an economy of full employment. They claim that many persons who would otherwise have been unemployed have been put to work at forced labor on a variety of governmental projects (such as the White Sea Canal, the Baikal-Amur Railroad, and the Turksib Railroad). These workers, whose numbers are estimated at 4,000,000 or 5,000,000 by some writers and as high as 17,000,000 or 18,000,000 by others, are employed under the most miserable conditions imaginable. In ordinary industries, large numbers of workers are employed at extremely low wages and a subsistence standard of living. These workers would probably be unemployed if decent wages had to be paid, it is argued, for their present low wages, if paid according to the value of the workers' services, indicate that their products are of very slight value to the economy as a whole. The Russian economy appears to have no unemployment because of these factors and because workers, when they become unemployed, are not allowed to clutter up the streets of the industrial cities. Instead they are sent back to the farms, and it is in agriculture that unemployment shows itself—not in the form of completely idle workers, for it is easy to appear to have something to do on the farm, but in the form of an excessive and unnecessarily large labor supply. Collective farmers were given plots of land for their own use partly because they were not fully employed on the collective farms, and even under the stringent regulations of recent years the collective farmers have only been required to spend 80 to 150 days per year in working on the collective farm land. This suggests that the collective farms could have gotten along successfully with much less labor than was actually available for them in most years. Thus, it is contended that unemployment is merely disguised, and not eliminated, in the Russian system.

On the other hand, there is no doubt that the market demand for skilled and trained workers in Russia has exceeded the market supply under the planned economy. Although almost six million skilled workers had been trained under the first two Five-Year Plans and many more from 1937 to 1940, a decree of 1940 provided for the conscription and mobilization of all boys of 14 and 15 years of age for training in vocational and transport schools, and of boys of 16 and 17 years for training in factory schools. In 1941, girls of 14 to 17 years were mobilized for training in commercial schools. The pupils were fed, clothed, and housed at governmental expense, and were to make restitution by serving as soldiers of industry for four years at ordinary wages in the government plants to which they were assigned. The courses of training varied in length from six months to three years and the mobilizations were supposed to affect from 800,000 to 1,000,000 young persons in each year.<sup>21</sup> These training programs operated through the war period and have been extended into the postwar period. Quite apart from any conditions of labor shortage or surplus in particular fields, there would seem to be no good reason why the Russian planned economy cannot furnish virtually full employment for labor if the leaders strongly desire to do so.

*Population Policy in Russia.* The population of Russia is not only large but, in normal times, growing rapidly. It increased from 139.3 million in 1913 to 154.2 million in 1928, 165.7 million in 1932, and 193 million in 1940 after the absorption of Latvia, Estonia, Lithuania, and other areas into the Soviet Union. The birth rate in Russia has remained steadily high at about 40 per thousand of population. However, Russia, unlike the fascist countries, is said to have no governmental policy of stimulating population growth and the leaders of the system would attribute the rapid growth of population to the favorable economic and social conditions which prevail in Russia. Among the conditions favorable to population growth are free medical attention and allowances to help out with the expenses attending childbirth, the certainty of employment for parents who need it, social security and the accompanying freedom from fear and worry, and the basing of marriage and the family on the secure foundation of love and affection rather than economic considerations and expediency. On the other hand, Russia has maintained in recent years some of the measures which are part of the

<sup>21</sup> *Foreign Commerce Weekly*, January 18, 1941, p. 105.

population policies of the fascist countries. For example, in 1936, Russia began to pay bonuses of 2000 rubles per year for five years for each child beyond the sixth in individual families, and bonuses of 5000 rubles for one year and 3000 rubles per year for four additional years for each child beyond the tenth in individual families. Such developments suggest rather clearly that the leaders of the country are definitely anxious for Russia to have a rapidly growing population.

#### QUESTIONS

- 1 How are wages, hours, and working conditions for labor determined under capitalism? Explain
- 2 "The citizens of the United States as a group have not always been willing to accept the wages, hours, and working conditions, produced by the operation of market forces, as entirely satisfactory" Explain
- 3 How do you account for the formation of labor unions among the workers under our capitalistic system?
- 4 "With some conspicuous exceptions, employers in the United States have been bitterly opposed to the growth and development of labor unions" Show whether you agree
- 5 "Business cycles, which produce such a tremendous volume of unemployment for workers are peculiar to capitalistic economic systems" Do you agree? Explain
- 6 "During World War II, labor in the United States was subjected temporarily to rather vigorous governmental controls" Explain
- 7 "In the postwar period, the federal government of the United States can and should guarantee full employment to its citizens without interfering with any other phases of the economic life of the country" Discuss
- 8 Discuss the adequacy of the social insurance system of the United States and the economic issues involved in the extension of the system
- 9 How would the wages, hours, and working conditions for labor be determined under a system of modern socialism? Explain
- 10 "We cannot conclude in an offhand fashion that real wages would be higher in a socialistic economy than in a capitalistic economy" Show whether you agree
- 11 "Other things equal, the great masses of workers should be better off under socialism than under capitalism" Do you agree? Explain
- 12 "There would be no place for labor organizations or unions under modern socialism" Show whether you agree
- 13 "A really comprehensive and adequate system of social insurance can be operated only under modern socialism" Do you agree? Explain

- 14 Only incredible stupidity would permit any significant volume of unemployment to exist for workers or other productive resources under socialism" Show whether you agree
- 15 "The wages, hours, and working conditions of Soviet Russian workers are normally very favorable, though they have changed for the worse in recent years" Explain
- 16 How are wages, hours, and working conditions determined for the workers of Soviet Russia?
- 17 The wages hours, and working conditions specified by laws and collective agreements in Soviet Russia are meaningless except as a device for deceiving outside observers of the Soviet system? Show whether you agree
- 18 How has the Soviet Russian system attempted to cope with such problems as excessive labor turnover, absenteeism, and lateness to work? Explain
- 19 How do the real wages and standards of living of Soviet Russian workers compare with those of the workers of leading capitalistic countries?
- 20 How would you evaluate the labor unions of Soviet Russia and their functions?
- 21 Soviet Russia has a comprehensive and adequate system of social insurance. Do you agree? Explain
- 22 "Soviet Russia has succeeded in eliminating unemployment" Show whether you agree
- 23 "Unlike the fascist countries, Soviet Russia has no governmental policy for stimulating population growth. Do you agree? Explain
- 24 Someone has said "If the government assumes responsibility for a person's welfare, it is also likely to assume responsibility for that person's conduct" Does the status of workers in Soviet Russia tend to support or contradict this conclusion? Explain
- 25 "Since workers today tend to stress security above other objectives the workers of Soviet Russia with their guaranteed employment, full social security and relatively equal wages, must be very well off from the economic point of view" Do you agree? Explain

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## CHAPTER 18

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### **THE STATUS OF LABOR**

*(Continued)*

#### *The Status of Labor in Britain under Partial Socialism*

THE British civilian labor force at the end of 1947 included some 18,905,000 workers. Out of this total, 7,263,000 workers, or over 38 per cent, were in manufacturing, 2,368,000 were in the distributive trades, 1,439,000 worked in transportation and shipping, 1,356,000 were in building and civil engineering, 2,073,000 held positions in either central or local government, 1,091,000 worked in agriculture, 1,114,000 were in the field of professional and personal services, and 828,000 worked in mining and quarrying.<sup>1</sup>

*Wages, Hours, and Working Conditions* Except for governmental interference, the basic wages, hours of work, and working conditions of British labor result from bargaining between workers and employers. The bargaining is collective in a great many cases, and in recent years this has increasingly meant the negotiation of national agreements, covering whole industries, between unions (or groups of unions) and associations representing the employers. In many other cases, negotiations occur on a district basis between the union and a district organization of employers. Normally the collective agreements have no time limit, and changes can be brought up for consideration at any time by either side, provided due notice is given.

British workers have made some gains in regard to wages and hours of work under the auspices of the Labor Government. Wages had been fairly well stabilized during the period of World War II and, for about a year after the end of the war, wage increases were

<sup>1</sup> *Labor and Industry in Britain*, March, 1948, p. 17

rather common. The average weekly earnings of all workers increased from 96 to 101 shillings between July, 1945, and October, 1946. Then there was a period of relative stability until the middle of 1947, followed by another burst of wage increases in the second half of the year. At the end of 1947, the average level of full-time weekly wage rates was nearly 5 per cent higher than at the end of 1946 and 73 per cent higher than in September, 1939. In a number of industries, hours of labor were reduced during the year without any corresponding reduction in weekly rates of wages. This had the effect of increasing hourly rates of wages. It is estimated that average hourly rates at the end of 1947 were 9 or 10 per cent higher than at the end of 1946 and 84 or 85 per cent higher than in September, 1939.<sup>2</sup>

Early in 1948 the government decided that such increases in wages could not go on without adding fuel to the fires of inflation, and it embarked on a policy of wage stabilization. Coincident with the introduction of a new and more stringent system of price control, the government called on British labor for the stabilization of wages at existing levels. While the government did not propose to interfere directly to secure the desired result and while it was not considered necessary for all individual incomes to be stabilized at existing levels, the government did argue that there should be no further general increases in the level of personal incomes without at least a corresponding increase in the volume of production. It called on all persons engaged in wage negotiations to keep this principle firmly before them and to act together on sound and public spirited lines in order to avoid a prolonged setback to Britain's recovery. Organized labor in Britain, acting through the Trades Union Congress, approved the proposal for wage stabilization on condition that the government pursue vigorously a policy designed not merely to stabilize but to reduce profits and prices.

Since the widespread reduction in the basic work week which had occurred in the first two years after World War I, there had been comparatively little change in hours of work until 1946, when over 2,000,000 employees secured a reduction in their basic hours. The reductions continued in 1947 and over 5,000,000 workers had their basic weekly hours reduced by about  $\frac{3}{4}$  hours on the average. Most of the reductions were from 47 or 48 hours per week to 44. This did not necessarily mean that the workers put in fewer hours,

<sup>2</sup> *Ibid.*, pp. 18-19.

since the national need for high output led workers in some industries to agree voluntarily to work overtime. In the middle of 1947, the average weekly hours worked by all workers in Britain were 45.0, as compared with 47.5 in 1945 and 46.5 in October, 1938.

**Controls Affecting Labor** During World War II, the activities of labor in Britain were subject to a considerable number of governmental controls. Wages were controlled, workers were virtually frozen to their jobs in essential occupations under the Essential Work Orders, control over engagement compelled those seeking work (with limited exceptions) to obtain it only through Employment Exchanges of the Ministry of Labor, strikes and lockouts were made virtually illegal, and labor disputes had to be settled on the basis of compulsory arbitration. However, the government gave a pledge to the trade unions to remove all wartime controls over labor as soon as possible after the war was over, and most of them were actually eliminated within a relatively short time.

In 1948, British labor was once more functioning under some governmental direction. During the economic crisis of 1947, the Control of Engagement Orders were reintroduced. This means that persons leaving their jobs can take new ones only through one of the Ministry of Labor's Employment Exchanges, and people seeking work can be given suggestions as to the occupations into which they should go, can be kept out of nonessential occupations, and, when necessary, can be directed to take jobs in essential industries. Moreover, in spite of the fact that the trend in the basic work week had been downward since the war, the government decided that it must ask for longer hours of work wherever they could contribute to increased production. The coal miners were one group which was asked to put in such extra time, and they now do so under varying arrangements. In some cases the miners work an extra shift each week or each fortnight. In others, they work an extra half hour each day.

The wartime system of compulsory arbitration of labor disputes was never abandoned after the war and British workers are still subject to it. Disputes between workers and employers are settled through voluntary collective bargaining machinery where possible. In case a dispute cannot be settled, a strike or lockout is illegal unless the dispute is referred to the Minister of Labor and he fails to settle it or refer it to the National Arbitration Tribunal within a

period of 21 days Members of the Tribunal are drawn from a list of appointed members (independent persons) and panels of persons chosen to represent employers and workers by the Minister after consultation with labor and management organizations In any given case, the Tribunal is made up of three appointed members, one of whom is Chairman, and two other members, one from the employers' panel and one from the workers' panel Neither of these panel members may have any direct connection with the industry involved in the dispute The decisions of the Tribunal are binding upon both parties to a dispute and become a part of their existing contract

Employers and workers are also subject to a governmental control, carried over from wartime, which makes the conditions achieved by collective bargaining the legal norm in each industry Under the wartime Order providing for the compulsory arbitration of disputes between workers and employers, all employers were required to observe, as a minimum, the "terms and conditions operating in each industry in each district," which meant for the most part the terms and conditions achieved by collective bargaining Thus an employer whose own workers were unorganized and who did not operate under any collective agreement with his workers would still have to observe the terms and conditions reached by collective bargaining in other parts of the industry The life of this control has been extended through 1950

*Labor Unions in Britain* British workers are still free to be members of labor unions under partial socialism, and many of them do so In fact, membership in unions reached an all time high of 8,714,000 at the end of 1946 This represented an increase of 911,000 or 11.5 per cent during the year<sup>4</sup> British labor unions include the two famous types, craft and industrial, and also some "general" unions which take in skilled, semi-skilled, and unskilled workers from all sorts of industries and businesses The labor unions are centralized at two levels, through federations and through the Trades Union Congress

Federations of unions cover a large number of unions in certain industries, as, for example, the Confederation of Shipbuilding and Engineering Unions of the United Kingdom The federations are coming more and more commonly to act as the unit for wage negotiations, though final decisions as to actions in labor

<sup>4</sup> *Ibid.*, p. 22

disputes are usually left to individual unions. At the same time, individual unions or federations may affiliate with the one national organization, the Trades Union Congress. In dealing with employers, the unions or federations retain their independence, though the General Council of the Trades Union Congress may be asked to intervene when a serious deadlock or dispute threatens. At the end of 1946, the membership of unions affiliated with the Trades Union Congress was 7,540,397, or 84 per cent of all trade union membership in Britain.<sup>5</sup>

The functions of labor unions in Britain include about all of the usual list, though some of these functions are likely to be less important under socialism than they were previously. The unions bargain collectively for their members on matters relating to wages, hours, and working conditions, but within the limits set by general governmental policies affecting these same matters. In disputes with employers, the unions may use the traditional labor weapons, such as strikes and picketing, provided that the Minister of Labor does not step in to settle the disputes on his own power or refer them to the National Arbitration Tribunal. Actually, work stoppages due to industrial disputes are not very common in socialist Britain. The number of such stoppages which began in 1947 was less than in 1946, though the number of workers affected and the total number of working days lost were slightly greater. The total number of working days lost from V-J Day through 1947 was about 6½ million, as compared with 65½ million lost in the corresponding period after World War I.<sup>6</sup>

British labor unions play a fairly important part in the management of various industries and businesses, though a variety of organizations set up for the purpose, but very often the ultimate control lies in the hands of the government rather than in those of management and labor. The unions play a minor part in the administration of social insurance schemes and carry on the usual educational, recreational, and social activities for their members. And, finally, the unions play an active part in the political activities of the country. They are free to devote union funds to political purposes and are the strongest single force in the Labor Party. In 1945, labor union membership in the Labor Party amounted to 2,510,000, or 82 per cent of the Party's total membership. However, after the

<sup>5</sup> *Ibid.*, p. 23

<sup>6</sup> *Ibid.*, pp. 20-21

1945 Parliamentary election, only 119 seats out of the 393 gained by the Labor Party, or about 30 per cent, were held by union members.<sup>7</sup>

*Unemployment in Britain* The record of socialist Britain in connection with unemployment thus far has been very favorable. In the transition from wartime to peacetime production, the Labor Government tried to make sure that war industries were closed down and non-war industries allowed to reopen or develop according to priorities that would allow the ex-war workers to be absorbed without any gaps in their employment. The policy could not be carried through perfectly, but the elaborate facilities of the Ministry of Labor and the long experience of its Employment Exchanges in handling labor movements kept unemployment to a minimum. The small figure of 103,000 unemployed in mid-1945 increased only to 362,976 in December, 1946, and then fell to 277,245 in December, 1947, or 15 per cent of the labor force.<sup>8</sup> It is too early yet to make any long-run appraisal of the success of socialist Britain in providing employment for its citizens, but there is no apparent reason why an economic system as thoroughly planned and controlled as Britain's is today should not be able to maintain employment at high levels if this achievement stands high on the list of objectives of the country's leaders.

*Social Insurance in Britain* British workers and other citizens enjoy a very complete and comprehensive system of social insurance and social services in general. Unemployment benefits are paid for 180 days and then are subject to review by tribunal. Sickness benefits are paid for an unlimited period of time if the beneficiaries have paid in 156 weekly contributions. Retirement pensions begin at age 65 for men and age 60 for women. Benefits in connection with unemployment, sickness, and retirement are all of the same size. In 1946, they ran 26 shillings weekly for single adults, with 16 shillings additional for an adult dependent, and 7 shillings, 6 pence additional for the first child (other children receive children's allowances). Injured workers receive injury allowances and treatment until able to return to work. If permanently disabled, either totally or partially, they receive industrial pensions which are based on degree of disablement and not on loss of earning power. No deduction from the pension occurs on account of what the disabled may

<sup>7</sup> *Labor and Industry in Britain*, January, 1947, pp. 16-17

<sup>8</sup> *Labor and Industry in Britain*, March 1948, pp. 17-18

be able to earn for themselves later on. The industrial pensions run from 9 to 45 shillings a week as the degree of disablement increases from 20 to 100 per cent.

In addition to these standard types of social insurance, the British system includes free and comprehensive medical service (including medical, dental, specialist, and hospital services), maternity allowances, maternity grants, allowances for attendance on confined women, death grants, widowed mothers' allowances, widows' pensions, guardians' allowances, and family allowances. The family allowances provide a weekly cash sum to mothers for each child after the first who is under the school-leaving age. In addition, the children receive daily allowances of free milk at school and free or cheap school lunches. This completes the list of social insurance activities proper, but the government carries on many other activities which fall under the broader heading of social welfare. These include a host of welfare activities for children, the prevention of cruelty to children, youth organizations and recreational facilities, activities catering to the special welfare needs of old people, special aids for the handicapped, protection of the food supply from contamination and adulteration, sanitation and sewerage regulations, provision of adequate pure water, workshop and factory regulations, the provision of housing, and activities in connection with town and country planning.

The total cost of the program of social services (including social insurance proper) is estimated at £511 million for 1948 and is expected to increase to £601 million by 1958. Of the £511 million in 1948, £21 millions were to come from interest on the reserve fund, £138 millions from employers' contributions, £175 millions from government funds, and £177 millions from the contributions of insured persons. Employed men over the age of 18 paid four pence weekly in 1946 for insurance against industrial injuries, and four shillings, seven pence weekly for the other features of the program. Different rates of contribution were paid by self-employed men and men not gainfully employed, and by males under the age of 18 in all these categories. There was a completely separate rate structure for women according to whether they were over or under 18 years of age and were employed, self-employed, or not gainfully employed. As the discussion of rates and other matters suggests, all persons are covered by the system and are covered literally from the cradle to the grave. Moreover, we should note that a great deal of the program

of social services has been set up by the present Labor Government.<sup>9</sup> *Real Wages and Standards of Living in Britain*. Except for the expansion of the program of social services, the watchword in connection with real wages and standards of living in three years under partial socialism to date has been "austerity." Money wages have increased but so have the prices of consumable goods and services. Taxes have taken a heavy toll of workers' incomes. Industrial production has recovered in many lines, but not enough, and large quantities of goods badly needed at home have been exported because of the crisis in international trade and foreign exchange. The same crisis led to reductions in imports of essential foods and other commodities. Strict rationing of foods, clothing and other commodities has continued to be necessary, and Britain has remained dependent upon outside assistance to maintain even the existing meager standards of consumption. So far, of course, the lack of progress in the matter of real wages and standards of living in Britain can be blamed on the postwar economic emergency, if one wishes, but there is no doubt that the progress in this field under British socialism still remains to be made.

*Conclusion on the Status of Labor in Britain*. On the whole, the treatment of labor in Britain under partial socialism has been rather favorable. In fact there are many outside observers who think it has been more favorable (1) than the postwar situation has warranted and (2) than can be maintained in the long run under socialism. With regard to the first of these points it is often asked how one can justify increases in money wages, reduction of basic weekly work hours, and embarkation on a comprehensive and very expensive program of social services in the midst of an economic emergency when production is falling short of needs and, in some cases, even short of immediate targets, when exports are continuing to fail to cover imports, when many goods are in short supply and strict rationing is necessary, and when the country as a whole is so dependent on outside assistance. Without appearing to oppose labor gains, it is possible to ask whether they could not have waited until a more appropriate occasion.

The second point is also easy to understand. Can labor unions be left free to bargain collectively in the long run and work out their

<sup>9</sup> This information on social insurance and related matters has been taken from *Social Services in Britain*. New York: British Information Services, 1947.

own destiny in matters of wages, hours, and working conditions in a planned and controlled economy of socialism? If they succeed in working out hours and wages which are inconsistent with the fulfillment of the government's plans for the whole economy, will they not be asked or compelled to give way to the larger national interest? Can unions protect the interest of their members if they are not allowed to use strikes and other weapons of labor but are compelled to submit to the arbitration of industrial disputes? Can the government maintain full employment for labor without also interfering seriously with the freedom of action of the individual workers on such matters as, for example, the taking or changing of jobs? Will problems of absenteeism, lateness to work, and loafing on the job arise under the system of guaranteed employment and full social security for workers, and, if so, will they not require additional, severe governmental controls over the individual workers? Will the British not discover that a government which sets out to confer all manner of benefits on the workers will eventually have to exercise control over the workers? Answers to these questions will be obtained only as the British economy gains more experience in operating under socialism.

### *The Status of Labor under Fascism*

All matters pertaining to labor were brought under strict governmental control in the fascist economies of Italy and Germany. The first step in the process was the liquidation of existing labor organizations. This was accomplished by simple and direct methods. In many cases, union leaders were arrested and jailed as enemies of the people, union offices and facilities were smashed and broken up, and union buildings, funds, enterprises, and activities were taken over by the government. In this way the fascists eliminated trade unions, collective bargaining, strikes and lockouts, and class warfare in general.

*Fascist Organizations of Workers and Employers.* The next step was the establishment of official governmental organizations for the workers and employers. In Italy the syndicate was the basic unit for the carrying on of employer-employee relations. The government permitted only one syndicate for each industrial category of workers or employers in each local geographical unit. Thus, in a given local area, there would be syndicates of workers in the clothing industry,

In the food-products industry, in the paper and printing industry, and so on, and also syndicates of clothing manufacturers, of manufacturers of foodstuffs and allied products, of paper manufacturers, and others In order to be legally recognized, a workers' syndicate had to include at least 10 per cent of the workers in an industrial category in a given local area and an employers' syndicate had to include enterprisers who employed at least 10 per cent of the workers in an industrial category in a given local area Both types of syndicates were to look after the educational and moral as well as the economic interests of their members, and the directors and officers of each organization had to give evidence of competence, character, and strong national convictions Both types of syndicates represented all the workers and employers in the given industrial categories, and were allowed to collect dues from all workers and employers, whether or not the workers and employers were actually members of their respective syndicates

The local syndicates of workers and employers in various industrial categories were gathered together in separate provincial, inter-provincial, and national federations Then, at the top, all the employers' organizations were combined into four confederations, namely, industrialists, agriculturists, merchants, and employers in credit and insurance All the workers' organizations were combined into five confederations, which included industrial workers, agricultural workers, workers in commerce, workers in credit and insurance enterprises, and professional men and artists

In Germany a new single organization, the Labor Front, was set up almost as soon as the fascists came into power, though the decree which provided for it officially was not issued until October, 1934 The Labor Front, however, was anything but a true labor organization In fact it was more nearly a section of the German fascist party Its leader, Dr Robert Ley, was a high party man, and he appointed all other officials of the organization The territorial organization of the Labor Front was exactly the same as that of the party, and its funds were handled by the party treasurer Membership in the Labor Front was voluntary in theory but compulsory in practice In normal times it had about 30,000,000 members, or something like six times the former membership of the trade unions

The non-union character of the Labor Front was also indicated by two other factors First, employers and professional men, as well as workers, belonged to the organization The Economic Chamber,

the National Agricultural (Food) Estate, the National Transportation Council, and the National Chamber of Culture all "belonged" to the Labor Front. Thus the organization was really a gigantic national "company union." Second, it made no attempt to improve the economic position of its employee members by means of collective bargaining with employers concerning wages, hours, and other conditions of employment. Indeed, its functions did not seem to be greatly concerned with employer-employee relations. It operated a large number of business enterprises most of which had been operated formerly by German labor unions. It furnished vocational training and cultural education for the workers, provided assistance for members in times of emergency, assisted in settling labor disputes, attempted to promote "understanding and solidarity" between workers and employers, sponsored the "people's car" and the "people's tractor," and propagated the Strength through Joy and Beauty of Work movements. Many similar activities were also carried on by the syndical organizations in Italy.

*The Determination of Wages, Hours, and Working Conditions.* In the fascist countries, the wages, hours, and working conditions of the workers were determined by the employers, except to the extent that the government saw fit to intervene. In Italy, a great show was made over collective bargaining by the syndical organizations and the drawing up of collective agreements governing the conditions of employment. Many of the collective agreements were negotiated at the federation level and were therefore provincial, inter-provincial or national in scope. Agreements between individual employers and their workers had to conform to the collective agreements which were larger in scope, except in the matter of provisions which were more favorable to the workers than those of the more general agreements. The collective agreements covered wages, hours, working conditions, vacations, and many other matters, and were binding on all employers and workers in the various industrial categories, whether or not these individuals were actually members of the syndical organizations. The collective agreements had to be approved by the government before they could go into effect.

The joker in this situation was that the workers' syndical organizations were not controlled by the workers and were nothing more like motley resembling labor unions. The workers had to pay dues to the syndical organizations and were bound by the wages, hours, and working conditions specified in the collective agreements which were

negotiated, but they were allowed to hold only subordinate positions in the syndical organizations. The higher officials were of "safe" middle class origin and were not infrequently party members appointed by the government to direct the syndicates. If they were not appointed from above, they were railroaded into office by means of manipulated elections. However, these same high officials of the workers' organizations "represented" the workers in the negotiation of collective agreements. As a result, these agreements were really contracts between representatives of the employers and representatives of the ruling bureaucracy and were not the result of genuine collective bargaining. Hence, in general, the employers were allowed to treat the workers as they pleased as long as the interests of the state were not endangered.

In Germany there was no fuss about collective bargaining and collective agreements. The National Labor Law said that in each plant the enterprise as "leader" of the establishment and the salaried employees and wage earners as "followers" must work together for the furtherance of the purposes of the enterprise and for the commonweal of the people and the state. The leader had absolute authority in the conduct of all affairs of his enterprise as long as he did not break any laws. The leader made decisions over against the followers in all matters relating to the business and, in particular, in the fixing of all labor conditions. By himself, or after consultation with his Confidential Council in plants employing 20 or more workers, the employer laid down works or establishment ordinances binding on all members of the enterprise. These ordinances covered such matters as the beginning and end of the working day and any breaks therein, times for the payment of wages and the nature thereof, principles for the calculation of piece rates, the nature, amount, and collection of fines, the grounds for discharge without notice (where permitted to the employer), and the utilization of pay forfeited by unlawful termination of employment.<sup>10</sup> Except as he was limited by general laws or decrees or was directly interfered with by officials of the regime, the employer was a law unto himself in determining wages, hours, and working conditions in his enterprise.

*The Settlement of Disputes and Protection of Employees.* In Italy, it was assumed that the workers were adequately protected against the employers by the collective agreements, but it was foreseen that

<sup>10</sup> R. A. Brady, *The Spirit and Structure of German Fascism*, p. 139.

conflicts of interest and disputes between workers and employers would arise. The fascist leaders were determined that these conflicts should not be allowed to lead to a cessation of production which might be harmful to consumers and to the interests of the nation as a whole. Consequently, under the Italian system of labor relations, workers and employers were forbidden to stage strikes or lockouts, or use any of the other weapons which employers and workers in capitalistic countries use in attempting to enforce their demands.

All labor disputes were supposed to be settled by arbitration or by court decision. Disputes between individual employers and workers were handled by ordinary magistrates or justices of the peace, assisted by two experts in the fields of production and labor. When collective disputes of some importance arose, arbitration was attempted by the federations and national confederations of the syndical organizations. If no settlement could be reached, disputes then went to the Ministry of Corporations, whose high officials attempted to bring about an agreement. Finally, the courts for handling collective labor disputes, called labor courts, were set up as special sections of the 16 courts of appeal. Each labor court consisted of three judges from the Court of Appeals of the district, assisted by two experts, one on labor problems and one on production. Before passing judgment on any labor dispute, the president of the labor court made one last (and frequently successful) attempt at conciliation. Where necessary, the labor courts decided the disputes on the basis of both law and precedent, and in consideration of the interests of consumers and of the nation as a whole.

In Germany several agencies were available for the protection of the workers and for the settlement of labor disputes, for the fascist leaders there also insisted on the maintenance of industrial peace. The Confidential Councils, groups of from 2 to 10 persons according to the number of employees, were supposed to afford some protection to the workers' interests in establishments employing 20 or more workers. According to the original method of selection, the employer, after consultation with the local party leader, would select a panel of "reliable" workers to be candidates for the Confidential Council. These candidates were then voted on by the workers and had to be either accepted or rejected as a group. If they were rejected, the Labor Trustee of the district would appoint the Confidential Council for the plant. In practice, the employers' can-

didates were so frequently rejected that the electoral feature of the system was eliminated after 1935.

The Confidential Council was supposed to act as an intermediary or buffer between the employer and the employees. Acting in an advisory capacity, it was expected to discuss measures calculated to increase the efficiency of the enterprise, to assist in the construction and enforcement of the works' regulations provided by the employer, to discuss the fixing of fines which were provided for in the works' regulations (such as those for lateness to work, uncleanliness, or smoking in the plant), and to assist in settling disputes in connection with the interpretation of the works' regulations or other matters.<sup>11</sup> The Confidential Councils had no power except that of appealing to the Labor Trustees, and, since the members were hand-picked, they probably had comparatively little influence on the employers' actions.

A more important limitation on the power of the employers was found in the fact that their regulations concerning wages, hours, and working conditions had to conform to the general rules and regulations laid down by the Labor Trustees. There was one Labor Trustee in each of the 14 industrial districts of the country. The Labor Trustees were not workers or workers' representatives, but were political appointees and usually trusted party men. They were supposed to maintain industrial peace in their districts and to settle labor questions which could not be settled within the individual firms. Specifically, the Labor Trustees appointed, removed, and supervised the constitution and activities of, the Confidential Councils, settling any disputes which arose, decided appeals from the Confidential Councils, quashed employers' rulings, and issued substitute ordinances, gave or withheld approval of mass dismissals of workers by employers, laid down general rules for works' regulations and supervised their observance, issued wage schedules and regulations and supervised their observance, cooperated in the exercise of jurisdiction by the Courts of Social Honor, and kept the government and party supplied with detailed information on a variety of questions.

The highest agencies set up to pass upon relations between employers and employees and to protect each group from wrongs committed by the other were the Courts of Social Honor, of which there was one in each of the fourteen industrial districts of the country.

<sup>11</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 164.

Each Court was composed of a member of the judiciary as chairman, a leader of a business (employee), and a member of a Confidential Council Appeals from the decisions of the Courts could be taken to the National Honor Court in Berlin The Courts could punish offenses against social honor by means of warnings, reprimands, fines not to exceed 10,000 marks, deprival of an owner or manager of the right to conduct his own or any other business, deprival of a member of a Confidential Council of the right to serve in this capacity, and dismissal of a workman or employee from his position

According to the Act for the Organization of National Labor, offenses against social honor should be deemed to have been committed in the following cases

1 When the owner of an undertaking, the leader of an establishment, or any other person in a position of supervision abused his authority in the establishment by maliciously exploiting the labor of any of his followers or wounding their sense of honor,

2 When a follower endangered industrial peace in the establishment by maliciously provoking other followers, and in particular when a member of the Council of Confidential Advisers in the establishment knowingly interfered unduly in the conduct of the establishment or continually and maliciously disturbed the community spirit within the enterprise,

3 When a member of the plant community repeatedly made frivolous and unjustified complaints to the Labor Trustee or obstinately disobeyed instructions given by him in writing,

4 When a member of a Confidential Council revealed without authority any confidential information or technical or business secrets which had become known to him in the performance of his duties and which had been specified to be confidential matters<sup>12</sup>

Malicious exploitation of labor included such things as unlawful overtime work, paying wages below the prevailing wage scales, undue speeding up of labor, providing unsanitary working conditions, and the denial of vacation rights Wounding the workers' sense of honor involved such things as arbitrary dismissal and the use of insulting language The other offenses on the list seem to speak for themselves

*Evaluation of Fascist Labor Organizations and Policies* It seems clear that the German and Italian workers under fascism were de-

<sup>12</sup> Act for the Organization of National Labor, Article 36, p. 11

pived of all the rights which they once had. They had no labor organizations worthy of the name, they had no right to bargain collectively in the usual way with their employers, they were allowed to use none of the weapons of industrial conflict to bring their desues forcefully to the attention of their employers, and the wages, hours, and working conditions which were so important to them were determined, for the most part, by the fiat of the employers and at their pleasure. Of course, the employers were also deprived of organization, lost the use of their weapons of industrial conflict, and were compelled to live in peace with the workers. However, anything like equal treatment for employers and workers left the employers with a decided upper hand.

Under the fascist systems, workers at times may have been well treated, but this result, if it occurred, was due to the good will and benevolence of the employers and not to the rights or activities of the workers. And if the fascist employers decided to treat their workers badly, there was virtually nothing that the workers could do about it so long as the employers did not actually break general laws or decrees or go against the will of governmental officials. The Confidential Councils in Germany, for example, were completely powerless to check the employers, and the Labor Trustees, as political appointees, were not much concerned with the question of justice for the workers. Their job was to maintain industrial peace so that production might continue smoothly and efficiently, and to see to it that the employers, in their domination of the workers, did not treat the workers so badly that national interests would be endangered.

The Courts of Social Honor in Germany and the labor courts in Italy did not seem to hold forth much hope for the workers. In the former courts, as we have seen, cases were decided by a judge, an employer, and a "reliable worker" (Confidential Council member) appointed by a Labor Trustee. Such a board could hardly be biased in favor of labor. The Italian labor courts were composed of three judges, assisted by two experts, one on labor problems and one on production. The regular judges of the labor courts were not likely to be pro-labor men, and the two experts were required to be college or university graduates, which meant, in Italy, that they were not likely to be biased in favor of labor. In the specification of the offenses with which the German courts could deal, the emphasis was clearly on offenses which workers might commit against the

employers, rather than those which the employer might commit against the workers. Moreover, if the workers brought cases against the employers and could not prove their points, the workers could apparently be punished for bringing "frivolous and unfounded complaints" against the employers.

Under these conditions, it is not really surprising that most of the cases actually handled by the labor courts of both countries were decided in favor of the workers. The employers brought relatively few cases to the courts because, under the fascist systems of employer-employee relations, the employers could get almost anything they wanted from the workers and could impose almost any conditions which they desired on the workers without resorting to the formalities of court procedure. Most court cases were decided in favor of the workers because, in the face of biased courts and severe penalties for unfounded complaints, the workers would not bring their cases to court unless they were so strong that even biased courts would have to decide in their favor. This meant, of course, that in the great majority of instances the workers merely swallowed their grievances and did not bring complaints to court. The courts, therefore, did not do a very rushing business. On the whole, there is no doubt that, from the workers' point of view, fascist organizations and policies in the labor field were exceedingly poor substitutes for labor unions, collective bargaining, collective agreements, and strikes.

On the other hand, there is considerable evidence that the employers were not entirely pleased with the fascist systems of labor relations. They were supposed to spy on the workers, and the workers might turn in adverse reports on the employers. Employers were expected to hire old (and not very valuable) party men and give them soft jobs. Employers could not hire new workers unless they had labor books and permits to change their jobs. Appeals to labor exchanges for workers were sure to bring party members if any such individuals needed jobs. Employers were controlled by governmental officials to a considerable extent and were often unable to offer increased wages to get the workers they wanted. They sometimes had to pay heavily, at the suggestion of party officials, to get lunch rooms, athletic fields, or shower baths constructed for their workers. They had to release their workers to work on certain governmental projects or attend party meetings, and pay their wages while they were away. They had to attend various meetings and demonstra-

tions and get their men to go. They had to contribute generously to charitable campaigns of the party and make up any deficiencies in their workers' contributions. These things suggest that life was not exactly a bed of roses even for the fascist employers.

*Wages, Hours, and Working Conditions.* As might have been expected, the wages, hours, and working conditions granted to the workers were none too favorable under fascism. Money wages in Italy were well maintained through 1926, but in the spring of 1927 a number of "spontaneous" cuts took place. In October, 1927, the government stepped in to bring about a general 10 per cent reduction in wages. From June, 1927, to December, 1928, wages in general fell 20 per cent. There was a further reduction of 10 per cent in 1929, another of 18 to 25 per cent by November, 1930, and still other adjustments in 1931. In 1934, wages were 30 to 40 per cent below the 1926 level. The cost of living also fell in the 1927-34 period, but not nearly so rapidly as wages.<sup>13</sup> In the following years of the Ethiopian campaign and of preparation for World War II, living costs rose sharply and wages as usual lagged well behind. After the entry of Italy into World War II, basic rates of pay for labor were blocked for the duration of the war at the rather unsatisfactory levels of July 30, 1940. However, increases of a sort in wages were permitted by means of family allowances for needy families, special premiums for industriousness, and supplementary payments to workers employed less than 40 hours per week. Employers contributed 10 per cent of gross payrolls for family allowances. Premiums for industriousness ran up to 120 hours' wages or a month's salary. The supplementary payments for short-hour workers amounted to 75 per cent of regular wages for the number of hours by which employment fell short of 40 hours per week.<sup>14</sup>

The labor laws set a nominal maximum working day of 8 hours, or 40 hours per week, but the many loopholes in the laws permitted widespread violations even in ordinary times and there was much overtime work without additional compensation. Other labor conditions were also none too favorable. Individuals were allowed to go to work for wages at the age of 12 years, and in the five-year period before the Ethiopian campaign the number of Italian workers between 12 and 15 years of age more than doubled.<sup>15</sup> Workers'

<sup>13</sup> C. T. Schmidt, *The Corporate State in Action*, pp. 80-81.

<sup>14</sup> *Foreign Commerce Weekly*, August 23, 1941, p. 12.

<sup>15</sup> W. Ebenstein, *Fascist Italy*, p. 167.

passes containing complete histories of the individual workers were adopted in 1933. Under the pressure of wartime conditions, wages and working conditions changed for the worse after 1940. The Minister of Corporations was empowered by a decree of July 16, 1940 to authorize the Inspectorate of Corporations to exonerate employers from the observance of labor restrictions imposed by various labor laws with reference to such matters as the night labor of women and children, the maximum of 10 per cent female employees in public and private offices, the Saturday half-holiday, the weekly day of rest, the 40 hour week, the weekly maximum of 12 hours of overtime work, and the labor of women and children in general.

In 1941, it was reported that the 48-hour week was very common, along with much overtime work, no half-holidays, and no rest on Sundays.<sup>16</sup> By a further decree of January 13, 1941, all persons regardless of age or sex working for a state-controlled plant producing war materials or for a private plant mobilized for the same purpose were made subject to military jurisdiction. The decree provided penalties of 6 months to 2 years imprisonment for absences from work without leave in excess of five days, 2 to 5 years' imprisonment for disorderly conduct, and especially for striking a superior technical or administrative officer, and the death penalty in cases of industrial obstructionism or sabotage.<sup>17</sup>

In Germany, total wages at the bottom of the post-1929 depression were 36 per cent below the 1928 level and more than 6,000,000 workers were unemployed.<sup>18</sup> From 1932 to 1936, there was a considerable revival of economic activity under National Socialism, but the workers did not prosper greatly. To be sure, average earnings per employed person increased from \$336.75 to \$372.78 per year during this period, but this result was due to the working of longer hours, for in this same period the average official tariff rate of pay for all skilled workers fell from 20.4 to 19.5 cents per hour while that for unskilled workers declined from 16.1 to 13 cents per hour.<sup>19</sup> Wage rates in many cases were set by the Labor Trustees and upward changes were seldom permitted. Workers were forbidden to ask for higher wages and employers could not offer them. In November, 1936, the diastic price-stop decree blocked wage rates, along

<sup>16</sup> *Foreign Commerce Weekly*, March 29, 1941, p. 529.

<sup>17</sup> *Foreign Commerce Weekly*, March 15, 1941, p. 442.

<sup>18</sup> *Facts in Review*, May 27, 1940, p. 212.

<sup>19</sup> W. R. Deuel, *People Under Hitler*, p. 307.

with other prices, at the levels then prevailing. At the end of the last peacetime year, 1938, weekly earnings of German workers were 31 per cent above those which had prevailed at the lowest point of the depression, but average hourly earnings were only 14 per cent above the depression low.<sup>20</sup> Money wages per week were very low all through this prewar period. In 1936, the earnings of all full-time employed workers of the Labor Front averaged \$6.95 per week, while the average earnings of all German workers were \$6.29 per week. Even in Berlin, the average earnings of all insured workmen amounted to only \$8.16 per week.<sup>21</sup>

Apart from the matter of wages, the situation of the German workers with respect to working conditions was fairly favorable in these prewar years. Nominally, the eight-hour day was fairly common in German industry, though the average work week in all industries increased from 41.46 to 47.04 hours from 1932 to 1938.<sup>22</sup> Working conditions could not be made too unfavorable for the workers, for the employers had to comply at least roughly with the rules and regulations of the Labor Trustees and were subject to penalties at the hands of the Courts of Social Honor if they treated their workers too badly. Moreover, the Beauty of Work movement, sponsored by the Labor Front, sought to secure "happy, beautiful work places" for the German workers. With funds furnished by the Labor Front and the employers, the Beauty of Work movement undertook such factory projects as redecoration and painting, ventilating and lighting systems, washrooms, dressing rooms, toilets, public rooms, dining rooms, reading rooms and libraries, auditoriums, gymnasiums, community houses, kindergartens for workers' children, swimming pools, athletic fields, playgrounds, gardens, and flower beds. On the other hand, after 1935, all German workers receiving less than 1000 marks per month were required to have work books as a necessary condition for employment. Such work books contained rather full histories of the workers, including such matters as apprenticeships, training, past positions held, present employment, date when employment began and type of enterprise, and any familiarity of the workers with driving, flying, and agricultural work. Work books were, in general, a means of increasing the effectiveness of governmental control over the workers.

<sup>20</sup> *Ibid.*, p. 306.

<sup>21</sup> *Ibid.*, pp. 308 and 313.

<sup>22</sup> *Ibid.*, p. 306.

After the beginning of 1938, conditions of employment for German workers changed for the worse Conscription of labor began in June, 1938 The head of the Employment Offices was given the power to conscript all types of workers (male or female, school students or aged persons, employers or ordinary workers, civil servants or business men) and put them to work for a period of six months or less in any industries and establishments where they were needed or require them to undergo vocational training Early in 1939, conscription was extended to include aliens, and the period of service was extended indefinitely

The beginning of war in September, 1939, brought further regimentation of labor Workers were forbidden to change their jobs unless they obtained official permits and gave three months' notice Wage rates were blocked at 1936 levels, holidays were suspended, and double pay for working overtime or on holidays was eliminated Former restrictions on hours of work for men, on night work for women, and on the employment of women and children under 18 years of age, were suspended Some of these developments were abandoned later on when they failed to have the desired effect of increasing production Holidays were restored and extra pay granted once more for overtime, night, holiday, and vacation work Special bonuses were granted for exceeding normal production, and some types of extra pay were made exempt from the income tax The working day was limited to ten hours, or twelve with special permission, night work for women and children was discontinued, and the working week for women and children was limited to 56 hours

*Real Wages and Standards of Living* There can be little doubt that the real wages and standards of living of Italian workers and their families, though they had always been low, declined somewhat under fascism In the period from 1926 through 1935, the decline in per capita consumption amounted to 10 per cent for wheat, 14 per cent for meat, 15 per cent for olive oil, 6 per cent for butter and lard, 21 per cent for sugar, and 11 per cent for fruits and vegetables Sales of tobacco were off 20 per cent, those of clothing and furniture 33 per cent, and so on The per capita consumption of meat was only one-half that of France, that of milk one-third, and that of butter one-sixth The poorest Italian people had very little to eat and some of them got along on one miserable meal per day of bread and greens One-third of the rural people lived in absolutely "unin-

"habitable" living quarters, sharing them hovels or caves with domestic animals. Half of the urban dwellings were without running water, one-third of them had no latrines, 95 per cent of them had no baths, and overcrowding was rampant.<sup>23</sup> The total shortage of housing was estimated at 9 million rooms, or 220 rooms per 1000 people.<sup>24</sup>

Even before the last few years of war or active preparation for war, Italy was said to have the lowest real wages of any country in Europe, and the average Italian diet had a lower calorific content than that of any other country in Europe except Poland. Although 3000 calories were considered a minimum, the average Italian diet provided only 2853 calories daily, and the average Italian consumed less meat, butter, eggs, and sugar than the average consumer of any other country.<sup>25</sup> Even a Fascist deputy, in an unguarded moment of parliamentary debate, declared "Our ration is perhaps the lowest in all Europe."<sup>26</sup> We cannot estimate just how much Italian real wages and standards of living were lowered by Italian participation in World War II, but since the production of armaments and war materials was emphasized and since the rations granted to consumers were rather steadily lowered, we can scarcely doubt that the Italian workers and their families made some further sacrifices.

There is some difference of opinion as to what happened to the real wages and standards of living of German workers and their families during the period before the beginning of World War II. Some official fascist agencies contended that there was some increase in real wages in this period, while others held that there was an appreciable decline. According to one outside source, the German national income increased by 33 billion marks between 1932 and 1938, but only 3 billion marks of this increase went to enlarge the consumption of the people, who themselves increased in number by 34 millions.<sup>27</sup> Whatever the trend in real wages may have been, it is certain that they could not have been very high on average money earnings which ran between 6 and 7 dollars per week, with the prices of many things as high, or almost as high, as in the United States.

<sup>23</sup> C. T. Schmidt, *The Corporate State in Action*, pp. 90-92.

<sup>24</sup> W. Ebenstein, *Fascist Italy*, pp. 184-185.

<sup>25</sup> *Ibid.*

<sup>26</sup> C. T. Schmidt, *The Corporate State in Action*, p. 90.

<sup>27</sup> *The Economist* (London), March 16, 1940, p. 455.

Moreover, the money earnings of German workers were subject to many types of taxes and deductions. According to the Reich Statistical Office, unemployment insurance contributions took 4.5 to 5 per cent of the workers' gross earnings, health insurance and pension contributions 5 to 5.5 per cent, and wage and poll taxes 3.5 per cent.<sup>28</sup> When various voluntary contributions were also deducted from wages, the total of taxes and other deductions amounted to something like 22 to 22.6 per cent for ordinary German workers.<sup>29</sup> And if one wonders why the German workers made large voluntary contributions out of their low money earnings, the answer is that many German workers and even business officials lost their jobs for not making adequate "voluntary" contributions to the Winter Relief Fund or other causes sponsored by the Party.

Before World War II, the average German consumed only 68 per cent as much beef and veal, only 57 per cent as much white bread, 51 per cent as much sugar, 47 per cent as many eggs, and 18 per cent as much mutton, as the average American. On the other hand, he ate 1 3/4 times as much cabbage, almost twice as many potatoes, more than four times as much rye bread, and 7 1/2 times as much maize-meal.<sup>30</sup> However, the real wages and standards of living of the German workers and their families undoubtedly compared favorably with those of Italian and Russian workers and their families. After the war began in earnest, great sacrifices were required of the German workers and their families, and real wages and standards of living declined significantly.

*Social Insurance* German and Italian workers, or those who were eligible, had all the common types of social insurance covering accidents, sickness, unemployment, old age, and other matters. In most cases, these types of social insurance were not instituted by the fascist regimes, but represented merely a continuation of what had existed previously. The social insurance systems were open to familiar criticisms. That is, many persons were excluded from some of the types of insurance, the benefits received by the insured were pitifully inadequate, and the cost of the insurance was borne to a great extent by the workers themselves. In Italy, at one time, only 5,000,000 workers out of 8,500,000 had unemployment insurance, the benefits ran from 6.25 to 18.75 cents per day, and only about a

<sup>28</sup> W. R. Deuel, *People Under Hitler*, p. 311.

<sup>29</sup> *Ibid.*, p. 311; M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 210.

<sup>30</sup> W. R. Deuel, *People Under Hitler*, p. 314.

south of the unemployed received the benefits<sup>31</sup> Old age and disability pensions ranged up to a maximum of \$10 per year.<sup>32</sup> In one year, expenditures for social services made up less than 1 per cent of total governmental expenditures, and the social insurance funds in general paid out only a little more than 40 per cent of their receipts, with the remainder being diverted to a number of other projects.<sup>33</sup> In Germany, before the war, pensions paid because of disability resulting from accidents amounted to 80 per cent of all benefits paid under the various social insurance schemes.<sup>34</sup> Thus there was many a slip between having a system of social insurance and actually receiving the benefits.

In connection with social insurance, we should also mention the *Opera Nazionale Dopolavoro*, or National Leisure Time Organization, in Italy, and its German counterpart, the Strength through Joy movement. Millions of workers in both countries belonged to these welfare organizations, which carried on a large number of activities for the benefit of the workers. The best-known and most showy activity was the provision of vacation trips at very low cost for the workers, but the organizations also carried on extensive athletic programs, sponsored concerts, plays, operas, vaudeville and moving picture performances, art exhibits, tours of museums and art galleries and other cultural and recreational events, and operated a program of adult education, giving instruction and training in a variety of subjects.

There can be little doubt that many of these activities were greatly enjoyed by the fascist workers, for they helped to make up for the workers' strictly controlled existence and the flatness of their purses. On the other hand, the workers had almost no freedom of choice or conduct in the activities, and they were the "beneficiaries" of a strong program of political education. That is, plays, films, concerts, operas, courses of training, and other activities were all "co-ordinated" with the fascist philosophy. The workers who participated in the activities usually had to be, or profess to be, true believers in fascism. From the point of view of the ruling party, the welfare organizations made sure that the workers were in a group as much as possible and were alone as little as possible. In this way the

<sup>31</sup> C. T. Schmidt, *The Corporate State in Action*, p. 83. W. Ebenstein, *Fascist Italy*, p. 168.

<sup>32</sup> W. Ebenstein, *Fascist Italy*, p. 174.

<sup>33</sup> *Ibid.*, pp. 166 and 174.

<sup>34</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, pp. 225-227.

workers were relieved of the temptation to do any independent thinking and were kept from getting into mischief in their spare time. The organizations were supposed to keep the workers reasonably happy and contented, so that they would be easier to govern and more productive in their work.

*Unemployment.* Since the basic means of production were owned privately in Italy and the workers had to depend on the owners for jobs, Italian workers were far from sure of having employment in the early years of fascism. Except in industries controlled by the government, the business enterprises like capitalistic employers elsewhere employed labor when it appeared that profits could be made and refused to employ it when business conditions appeared unfavorable. Even in fairly prosperous times, considerable numbers of workers were unable to find jobs, and the number of unemployed officially admitted reached 20 per cent of the former total number of wage workers at the bottom of the post-1929 depression. This estimate of unemployment is considered to be well below the actual total, since unemployed female workers were not included in the estimate and many jobless workers in the cities were sent back to their native villages where they could at least simulate being employed.

The Fascist reactions to the unemployment problem were, on the whole, capitalistic in character. Hours of employment were reduced in order to share the work, women were required to give up their jobs in order that men might be employed, the introduction of further technological changes was restricted, public works programs (averaging 2 billion lire per year from 1930 to 1936) were set in motion, and charity was dispensed by the Fascist Party and the syndical organizations. After 1935, conditions of actual war or active preparation for war resulted in the virtual elimination of the unemployment problem, except for the temporary unemployment which resulted as industries were changed over from peacetime to wartime production. However, it is obvious that there is nothing about full employment for war which is very beneficial for workers in general.

As we have seen, the number of unemployed persons in Germany reached 6,000,000 at the worst of the post-1929 depression, and the new fascist government, when it came into being, began a spirited attack on the unemployment problem. The devices used included the spreading of work by reducing hours, the absorption of unem-

ployed persons into the labor service and "land year", marriage loans and bonuses made on condition that the newly created wives did not resume employment, tax remissions for female domestic servants, grants to employers to get them to employ workers over 40 years of age with families instead of young workers, the prohibition of "multiple earnings" within the family, reintroduction of compulsory military service, tax concessions to employers to get them to repair or extend their factories and productive facilities in general, and an extensive program of public works. Regular employment increased from 12,730,000 to 14,540,000 in the period from June, 1932 to December, 1934, and substitute employment increased from 180,000 to 610,000.<sup>25</sup>

In later times, active preparation for war and finally war itself operated to eliminate the unemployment problem and to create a severe shortage of labor. In 1935, the Employment Office was given a complete monopoly over employment service, vocational guidance, and the placing of apprentices. By a series of steps, workers were tied securely to their jobs. Wives of soldiers were denied social insurance benefits if they were available for work but refused to accept employment. In 1937, women who received marriage loans or grants were permitted to return to employment. In 1938, every young woman was required to spend a year in the compulsory labor service before entering any ordinary occupation. All German women of working age, whether married or unmarried, were required to fill out work questionnaires in 1939, giving full details concerning their experience and capacities. The information gained in this way was used as the basis of a drive to force women into employment.

Workers who reached the retirement age after January, 1939, were not permitted to retire on old age pensions, and many workers who had already retired were compelled to return to active employment. After February, 1939, enterprises employing Jews were no longer subject to penalties, and businesses in general were urged to employ Jewish workers, where necessary, as quickly as possible. Even the prisons were opened in a drive to find workers. The Employment Office decreed in 1938 that compulsory labor should be introduced for all prisoners without regard for the nature of their crimes or the length of their terms of imprisonment. The convicts were employed primarily in quarries, brick factories, mining, cable

<sup>25</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 17.

laying, forestry, power plants, soil-conservation projects, road building, and canning factories. Employers paid the government 60 per cent of the normal wages in these trades for the convict labor, but were allowed to count the cost of the convicts' upkeep and then guards against the 60 per cent.

Workers were forced from the handicraft trades into industrial and business employments. Only registered master artisans were allowed to continue to operate their handicraft enterprises and, in 1939, further decrees deprived many thousands of handcraftsmen of the right to operate their businesses. These persons in over-crowded trades (bakers, butchers, hauddiseers, tailors, and shoemakers) had to seek employment in industry. Itinerant workers, such as hucksters, were made subject to heavy taxes and were deprived of the right to continue their businesses whenever it was thought that their labor would be more useful in industry. Extensive programs for training new workers and for retaining old workers were carried out. The conscription of labor, starting in June, 1938, was also intended to increase the labor supply available for industry and business.

As of the spring of 1939, shortly before the outbreak of war, there were 34,269,000 workers of all kinds employed in the old Reich, an increase of 29.6 per cent since 1933. Of these workers, 41.5 per cent were in industry, 27.3 per cent in agriculture and forestry, 17.2 per cent in trade and service, 10.2 per cent in public employment, and 3.8 per cent in household service.<sup>36</sup> However, even this large labor supply was inadequate to fill the needs of the economy. By the fall of 1941, the number of women workers had increased by another 10 per cent, 2,139,553 foreign workers had found employment in Germany and about 1,500,000 war prisoners had been set to work.<sup>37</sup> Later the numbers of foreign workers and war prisoners employed in Germany were greatly increased. On the whole, then, the German economy under fascism became as near to a full-employment economy as any country can be. However, we may well wonder what increases in employment are worth if they do not bring improvements in standards of living and consumption.

**Population Policy** The fascist regimes in Germany and Italy did everything in their power to bring about a rapid growth of population. This policy was in direct conflict with the interests of the indi-

<sup>36</sup> *Foreign Commerce Weekly*, May 16, 1942 pp. 67

<sup>37</sup> *Ibid*

vidual fascist citizens as consumers and seemed also to be in conflict with the fascist program of economic self-sufficiency. An attempt to be economically self-sufficient is always likely to be rather costly in terms of standards of living, but the burden imposed by such a program is likely to be smaller when it is carried on for a relatively small population than when it is carried on for a relatively large one. The population of the fascist countries was already large, and the pressure of population on land and other resources was used by the fascist leaders as a justification of their demands for territorial expansion. However, a large population was eminently desirable for military purposes, and this consideration outweighed all others in connection with the population policy.

The fascist population policy had many phases. The governments tried to prevent the migration of people from the country to the cities, since population ordinarily grows more rapidly in the rural areas. The government sought to repatriate fascist citizens who had emigrated in previous years and to reduce new emigration to a minimum. The program included prenatal care of mothers, the combatting of infant diseases, the training of mothers in proper methods of infant care, and outright provision for needy, abnormal, orphaned, or abandoned children.

Special honors were conferred on large families, and especially their mothers. Medals of iron, silver or gold were presented to mothers, according to whether their children numbered 4 to 5, 6 to 7, or 8 or more. The entire propaganda machine of the countries glorified maternity. Conspicuous achievements in fecundity won newspaper citations or radio broadcasts. Honor cards permitted the mothers of large families to receive prompt attention in governmental or party offices and to be waited on quickly in the stores. On the negative side, severe penalties awaited any person who criticized marriage or maternity; abortions were strictly forbidden and subject to heavy penalties, birth-control clinics were closed, and the use of contraceptive devices was discouraged and their advertisement and display forbidden. Even local governments cooperated by staging "baby derbies" and by furnishing premiums, medals, diplomas, cheap housing, free or cheap transportation services, low taxes, and low public utility rates to the more prolific families.

In attempting to ease the financial situation of the larger families, the fascists provided tax reductions and exemptions, higher wages and salaries, extra social insurance benefits, and scholarships for the

children of such families Bachelors were required to pay special taxes in order to retain their single blessedness Lump-sum grants of cash and continuing monthly subsidies were paid to the large families Finally, loans were made to newly married couples These loans had to be repaid in full if the couples remained childless, but were cancelled in part with the arrival of each child

It is difficult to evaluate the results of the fascist population policy In Italy the birth rate decreased as much in fifteen years under fascism as in the preceding fifty years, and the ratio of births to deaths decreased In 1922, the birth rate was 30.8 per thousand people, and the death rate was 18.1, leaving an excess of births of 12.7 In 1937, the ratio was 22.9 to 14.2, with an excess of births of 8.7<sup>28</sup> In other words, the population continued to increase but at a diminishing rate In the absence of any governmental policy with respect to population, however, the rate of population growth might have declined still more In Germany, the excess of births over deaths had fallen to 3.5 per thousand of population in 1933 at the worst of the great depression From 1934 to the beginning of World War II, the excess of births over deaths remained quite stable at 7.1 or 7.2 per thousand<sup>29</sup> However, this excess of births over deaths was not large in comparison with that of other countries, it showed no tendency to increase after making one jump from the depression low, and the increase might have occurred under improving economic conditions even if no formal population policy had been instituted On the whole, few outside observers gave much credit to the economic inducements, propaganda, and public honors in connection with population growth in the fascist countries

#### QUESTIONS

- 1 "British workers have made considerable gains in connection with wages and hours under partial socialism" Do you agree? Explain
- 2 "Have governmental controls over the workers increased or decreased in Britain under partial socialism? Explain"
- 3 "Labor unions continue to exist in Britain under partial socialism but the importance of some of their functions has diminished Show whether you agree"

<sup>28</sup> W. G. Weil, *Fascist Economic Policy*, p. 183

<sup>29</sup> E. R. Sikes, *Contemporary Economic Systems* New York: Henry Holt and Company, 1940, p. 326

- 4 "The record of socialist Britain in connection with unemployment has been very favorable thus far" Do you agree? Explain
- 5 Compare the social insurance system of Britain with that which exists in the United States
- 6 "Little progress in regard to real wages and standards of living was made in Britain in the first three years under socialism" Show whether you agree
- 7 "The former organizations of labor were quickly eliminated under fascism, but new ones were soon put in their place" Discuss
- 8 "The functions of fascist labor organizations were not the same as those of ordinary labor unions" Explain
- 9 How were labor disputes settled in the fascist countries? Explain
- 10 How were wages, hours, and working conditions determined in the fascist countries? Explain
- 11 "Most cases decided by the labor courts in the fascist countries resulted in victories for labor" Discuss
- 12 "The workers did not fare very well with respect to wages, hours, and working conditions under fascism" Show whether you agree
- 13 "The real wages and standards of living of the workers and their families improved greatly under fascism" Do you agree? Explain
- 14 "The criticisms directed at the fascist systems of social insurance were similar to those which apply to the social insurance systems of some other countries" Show whether you agree
- 15 Describe and evaluate the *Opera Nazionale Dopolavoro* in Italy and the Strength through Joy movement in Germany
- 16 Workers in the fascist countries were relatively sure of being able to find employment" Show whether you agree
- 17 "The results of the population policy in Germany and Italy indicate that it is rather easy for a dictatorial government to control the growth of population" Do you agree? Explain
- 18 "From the German workers point of view, the Labor Front Works' Regulations, Confidential Councils Labor Trustees and Courts of Social Honor were very poor substitutes for labor unions, collective bargaining, collective agreements, and strikes" Show whether you agree
- 19 "There are some reasons for thinking that even the employers were not entirely pleased with the fascist labor organizations and policies" Explain
- 20 The fascist economies had an advantage over our capitalistic system in that they succeeded in eliminating labor troubles and in securing peaceful employer employee relations" Discuss

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CHAPTER 19

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## INTERNATIONAL TRADE

### *International Trade under Capitalism*

**The Basis of International Trade.** As we have seen in discussing economic principles in relation to economic systems, the general principles of economics in the field of international trade are valid for all types of economic systems. In the first place, international trade depends upon differences between countries with regard to the productive factors which they possess. Countries differ with respect to the quantity and quality of land, mineral resources, timber, and power resources which they possess. They have different climates and different amounts of capital available for assisting in the various processes of production. Then labor supplies differ with respect to quantity, quality, and training. Differences in the endowment of productive agents between countries may be either absolute or comparative. When the difference is absolute, one country has agents and facilities for producing certain types of economic goods, but another country lacks these agents and facilities altogether. When the difference is comparative, both countries have the necessary agents for producing a certain economic good, but these facilities can be used for this purpose to much better advantage in the one country than in the other.

In a situation of absolute advantage, for example, the United States has excellent facilities for producing automobiles, while certain Central American countries, besides being short of workers having the proper skill and training and perhaps fixed capital as well, lack the necessary supplies of iron and coal which the United States has in abundance. On the other hand, these Central American countries can produce bananas or coffee with the greatest of ease, while these articles could be produced in the United States only with the greatest difficulty, if at all. In a situation of comparative advantage,

the United States has an abundance of land, labor, and capital suitable for the production of such a commodity as flax and could probably produce flax with greater physical efficiency than the countries from which it normally imports the flax or economic goods derived from it. However, the United States produces very little flax because the agents of production which could be used for this purpose can also be used in many other fields of production in which their marginal productivity is higher. The agents of production suitable for flax raising in other countries are certainly no better than those of the United States, and quite probably are not so good, but they can be profitably used for flax raising because their other opportunities for highly productive and valuable employment are limited. In this situation, the United States can profitably import flax, in spite of having great efficiency in its production, in order to reserve its own agents of production for other industries in which their productive efficiency is still greater than in flax raising.

Since differences in productive-factor endowments between countries lead to differences in the efficiency with which various economic goods can be produced from one country to another, they also produce variations in the cost per unit of producing these goods and opportunities for profitable trade between the countries. In the absence of restrictions and interferences, each country tends to produce and export commodities whose production requires (1) large quantities of productive agents which are abundant and cheap in that country and (2) small amounts of productive agents which are scarce and dear, while importing articles whose production requires (1) large amounts of agents of production which are scarce and costly in that country and (2) only small amounts of agents of production which are abundant and cheap. It is not economically advisable for a country to produce every type of economic good which can be produced there. In fact, it does not even pay a country to produce all types of economic goods which it can produce with greater efficiency than other countries. A country can often gain by giving up the production of articles which it can turn out only slightly more efficiently than other countries in order to use the productive agents, which would otherwise be devoted to these purposes, in other lines of production in which the advantages in efficiency with respect to other countries are greater.

The formal principle of economics which covers this situation, known as the Law of Comparative Advantage, states that *a country*

*tends to export those economic goods in the production of which it has a comparative advantage and to import those economic goods in the production of which it has a comparative disadvantage.* As this principle implies, every country, whether its agents of production are plentiful and high grade or the reverse, may secure an economic gain from international trade. International trade between two countries tends to make the prices of goods which are able to move between the countries the same in both places, except for costs of transportation. There is also a tendency (though less complete) toward the equalization of the prices of the different varieties and grades of the productive agents in the two countries when they trade with each other. If geographical specialization and the equalization of factor and commodity prices could be complete between countries, all endowments of productive factors would be used for the most appropriate purposes, and real income and standards of living would be at a maximum in the trading countries. Each country would gain by receiving from other countries economic goods which could not be produced at all in that country or which could be obtained more cheaply from the other countries. The effect of the complete development of international trade would be to remove the disadvantages which were originally imposed on the various countries by the unequal distribution of productive facilities among them. Even with a partial development of trade, this result is achieved to some extent.

The gains from international trade, although all trading countries share in them, are not necessarily divided equally among the countries. The extent of the gain realized by each country depends upon what has been called the play of reciprocal demand, or, in other words, the strength of the demand of one country for the economic goods which it imports as compared with the strength of the demands of other countries for the economic goods which the first country exports. If one country needs its imports from a second country very badly and cannot get along without them, while the second country does not care much about the goods obtained from the first country or could just as well get them from some other place, the terms of trade will be relatively unfavorable to the first country. Both countries will gain from the trade, but the greater share of the gain will go to the second country.

Actual conditions in international production and trade are more complicated than those assumed in the theory of trade. The agents

of production are not so thoroughly divisible as the theory assumes, they are not completely mobile within nations nor completely immobile between nations, the prices of finished goods are not always determined under competitive conditions, nor are all units of productive agents always rewarded according to their marginal productivity. Nevertheless there is a gain to be derived from international trade under actual conditions, and it is a gain of the sort indicated by our discussion above. However, the Law of Comparative Advantage does not suggest that each country has to receive a gain from international trade, whether or not it wants to receive a gain. If a country wishes to forego all or any gains from international trade, it is quite free to do so. It can attempt to cut international trade down to a mere trickle, or even eliminate it entirely in the interests of national self-sufficiency. The Law of Comparative Advantage does not imply that national economic self-sufficiency is impossible. It merely suggests that any country which becomes economically self-sufficient will do so at the cost of having a standard of living lower than that which could be readily secured on the basis of international specialization and trade.

Another principle of international trade is found in the statement that the imports of a country must equal its exports over any considerable period of time. This principle, unlike the Law of Comparative Advantage, is not one which a country can disregard if it wishes. Unless a country will import, it cannot continue to export in the long run except by giving its goods away to other countries. In similar fashion, if a country cannot find markets for its exports, it will be unable to secure the volume of imports which it desires in the long run. As a temporary expedient, imports can be paid for with gold or exports can be sold by extending credits to other countries, but international trade is fundamentally barter in the long run.

*Restrictions on International Trade.* It would not be very consistent for an economy to maintain a policy of laissez-faire with regard to domestic production, trade, and other economic affairs and at the same time to regulate and interfere with international trade to a great extent. For this reason a capitalistic economy, in strict theory, should be a free-trade economy. However, some groups of people, and especially the owners of industries which have established themselves or are trying to establish themselves in the economy, usually feel that their economic interests would suffer under

a policy of free trade. And these groups are more articulate than the great masses of consumers whose standards of living would be maximized by the free interchange of goods in international trade. Again, the people or the government of a capitalistic economy may decide that the interests of the nation as a political unit require a policy of restrictionism with respect to international trade, in order that the nation may be economically independent of other nations in times of war. If these reasons do not suffice, many others can be brought forward in support of governmental interference with the normal course of international trade. As a result, most capitalistic economies, whatever their policies with respect to domestic economic affairs, have interfered strenuously and continuously with international trade.

The devices used for this purpose are well known and we shall only mention some of them briefly. Historically, the most important device has been the protective tariff, under which various articles produced abroad are made dutiable at rates designed to exclude these products, so that the home market is left free for exploitation by domestic enterprises turning out the same types of goods. If, for example, a certain article can be obtained from England at a price of 75 cents per unit (including transportation costs) but cannot be produced in this country for less than \$1.00, then a duty of, say, 50 cents per unit is levied on this article so that our wants will be satisfied by products made at home, if satisfied at all. When similar duties of varying amounts are applied to hundreds or thousands of articles, the result is a protective tariff. While some goods may continue to be imported despite the duties which are applied to them, the purpose of the protective tariff is clearly the exclusion of foreign goods.

Sometimes the same result is achieved by paying bounties to domestic producers, which make it possible for them to sell their wares at prices below full costs of production. Such low prices for the domestic goods make it difficult for foreign producers to compete in the domestic market, and relatively easy for the subsidized producers to sell in foreign markets, other things being equal. It is also possible to protect domestic producers by means of sanitary regulations applied to imported food products, veterinary laws, regulations requiring that imported goods bear a distinctive mark indicating their country of origin, and regulations governing the granting of public contracts, which require that domestic materials must be used or

make it necessary for materials to come up to certain specifications which foreign materials can hardly meet. In modern times, international trade is often restricted by means of import quotas, or laws and decrees which limit (by value, quantity, or weight) the imports of certain articles that may enter a country within a specified period of time. Imports or exports of various articles may be forbidden unless the government grants licenses or permits covering the specific transactions. The government of an economy may also control imports and exports by controlling foreign-exchange transactions. Under one common type of foreign-exchange control, the government requires all exporters to sell all foreign-exchange bills to a central authority, which in turn sells foreign exchange to importers for the importation of desired goods. Other exchange devices, such as clearing agreements or payments agreements between countries, may be used to control the volume and content of international trade.

*The International Trade of the United States.* The United States, like most other capitalistic countries, has followed a policy of restrictionism with respect to international trade for many years, depending primarily upon the protective tariff for this purpose. For over a century and a quarter, the United States has maintained a protective tariff at varying levels, and in recent years this country has been an acknowledged leader of the restrictionist movement. What our policy of restrictionism has cost us cannot be estimated with any accuracy. However, the cost has been experienced in many forms, including lower standards of living for consumers, the devotion of productive agents to the production of protected articles which could be obtained more advantageously from abroad, instead of using these factors in our export industries where they would be more productive, the creation of international ill-will, and the default of many countries on their financial obligations to us because of their inability to export. While there have been some offsetting gains, they have gone for the most part to relatively small groups of people, and especially to the owners of the protected industries, rather than to the people as a whole.

The international trade of the United States has had its ups and downs, but it has remained very small in comparison with the total volume of domestic trade and in comparison with the volume of international trade which might have been achieved in the absence of the policy of restrictionism. In 1920, under the influence of post-

war conditions and the extension of large amounts of credit to other countries, our commodity exports reached \$8,228,016,000 and our commodity imports \$5,278,481,000. Our international trade was quite well maintained over the next several years, and in 1929 we still had exports of \$5,240,995,000 and imports of \$4,399,361,000. In the post-1929 depression, however, our exports fell to \$1,611,016,000 and our imports to \$1,322,774,000 in 1932.<sup>1</sup> In the years after 1932, in spite of the recovery of domestic production and trade and the adoption of a more lenient policy toward international trade under the Reciprocal Trade Agreements program, the international trade of the United States expanded relatively slowly until World War II broke out in 1939.

The general policy of restrictionism with respect to international trade has very little economic justification. We cannot pause to examine and evaluate the arguments which are advanced in favor of restrictionism, but practically all of them are wholly or partly invalid from the economic point of view. About the only argument of any standing holds that restrictionism is necessary to the national preparedness and defense of the country. According to this notion we should produce as many essential articles as possible within the country without too much regard for cost so that we cannot be cut off from our sources of supply in wartime. To attain national security is more important than to insure that our productive resources will be used most effectively or that the greatest possible sum total of commodities and services will be produced. But even this argument is open to some qualification. Restrictionism, as a narrow nationalistic policy, is a very prolific source of international ill feeling and friction. Moreover, while it may be granted that it is a very serious matter when our sources of supply of important materials are cut off in time of war, we must recognize that, if nations cooperated with each other and were greatly dependent upon one another on the basis of freedom of trade, the likelihood of war would be lessened to a marked degree.

In spite of the policy of restrictionism with respect to international trade, the United States has not sought to become economically self-sufficient in the past. Instead, we have depended upon other countries for all or part of our supplies of many economic goods, which have included rubber, tin, silk, manganese, nickel, chromite, tungsten, potash, antimony, mercury, tea, spices, coffee,

<sup>1</sup> *Statistical Abstract of the United States, 1939*, p. 463.

hides, jute, hemp, sisal, quinine, iodine, and many other products. Our dependence on other countries for supplies of vital materials became greatly embarrassing to us after our entry into World War II when many of our most important sources of supply were cut off.

After the war began, there was a great increase in the extent to which the international trade of the United States was controlled by the federal government. Even before this country entered the war, the government set out to accumulate stock piles of certain strategic and critical materials and entered into agreements with various Latin American countries for the purchase of all then available supplies of such materials. Moreover, after December 27, 1941, the government assumed complete control over the imports of a number of materials, and these things could be imported only by some governmental agency.

Our foreign trade was affected also by the "freezing" of foreign assets. The freezing process was based on an Executive Order administered by the Federal Reserve Banks and the Treasury Department, and it prohibited all transactions within the jurisdiction of the United States in which the country (or its nationals) to which the order applied had any interest, after a stipulated date. The freezing process, first used in April, 1940, was extended to country after country as German conquests continued, to Germany and Italy themselves in June, 1941, and to Japan in July, 1941. Naturally, all imports and exports between the United States and any country whose assets had been frozen were automatically prohibited, unless our government saw fit to issue licenses for specific transactions. This was also true of transactions between countries with frozen assets and any third country, if the transactions were to be financed by means of foreign credits held in the United States.

The freezing orders as such were not applied to Latin American countries, but something of the same effect was produced by the promulgation in July, 1941, of the Proclaimed List of Certain Blocked Nationals. This list contained the names of persons and firms believed to be nationals of or sympathizers with the Axis countries, and located in countries of the western hemisphere. Our government forbade all business and financial transactions between citizens and residents of the United States and listed persons or firms, unless specifically permitted by licenses issued by the Treasury Department. The United States had considerable cooperation from Latin American countries in carrying out this policy, which was

aimed quite definitely at depriving the Axis powers of any economic advantages they previously derived from enterprises, investments, and business connections in Latin America.

The exports of the United States were also subjected to direct control during the war period. In July, 1940, the National Defense Act provided for a general system of export control by means of licenses. This export control system was originally intended to apply to essential raw materials, machine tools, certain chemicals, arms, ammunition, and war goods in general. However, the list was increased rapidly, and soon scarcely anything included in our normal list of exports could be exported without a federal license. The export control system prevented other countries from buying here raw materials and goods which were needed in our war program, but permitted us to send all kinds of goods to countries of the western hemisphere which were collaborating with the United States in her war program. Even before our entry into the war, export control enabled us to interfere with and hamper the war activities of the Axis nations.

Finally, the lend-lease policy of the United States had an important effect on our trade. This policy was provided for in the Act to Promote the Defense of the United States, which was passed in March, 1941. This Act authorized the President to sell, transfer title to, lease, lend, or otherwise dispose of various defense goods to other countries whose defense was deemed vital to the safety of the United States. The Act specified that lend-lease aid could be given under any terms and conditions which were satisfactory to the President, and that the resulting benefit could be payment in kind or property, or any other direct or indirect benefit which the President deemed satisfactory. From March 11, 1941, to August 31, 1946, lend-lease aid to our allies amounted to over 50½ billion dollars and reverse lend-lease, or contributions of the allied nations to the United States, amounted to about 7½ billion dollars.<sup>2</sup>

Clearly, the various governmental controls just described did not all make for a decline in the total volume of our international trade. Some policies such as the lend-lease program and the overall purchasing agreements for strategic and critical materials, tended to increase trade. As a result, the total volume of the international trade of the United States, in terms of merchandise, increased from \$5,495,000,000 in 1939, to \$18,178,000,000 in 1944. The expanding

<sup>2</sup> *The Chicago Tribune*, November 18, 1946.

total trade in this period was largely the result of sharply increasing exports and lend-lease goods played a very important part in total exports In 1944, for example, exports were \$14,259,000,000 and imports only \$3,919,000,000, while lend-lease exports amounted to \$11,305,000,000<sup>4</sup> After 1944, the volume of international trade fell off considerably, though it still remained very high when judged by prewar standards Beginning in 1948, the Marshall Plan, a kind of peacetime version of lend-lease, was expected to bring about an increase in "trade" once more

### *International Trade under Socialism and Communism*

**Trading Policy** The Law of Comparative Advantage would apply as well to a socialistic economy as to any other, but it does not follow that a socialistic economy would be committed to a policy of complete free trade All the important domestic economic affairs of such a system would be conducted on a basis of economic planning, and uncontrolled imports, exports, and international financial transactions might have a most disrupting influence on the planned operation of the domestic economy The probable policy for socialism is therefore neither complete free trade nor complete restrictionism, but rather planned trade, and all imports and exports would be considered in their relationship to planned results at home On the other hand, it would be expected that a socialistic economy would plan to import some goods which could be obtained from other countries more cheaply than by domestic production, and export other goods with respect to which this relationship was reversed

In deciding on the relative cheapness of imported and domestic products, a socialistic economy would be probably somewhat handicapped by the rather arbitrary character of the costs of production allocated and assigned to the various goods produced at home, but it could take a genuine long-run point of view in making its decisions and would not be influenced by temporary considerations of profit or advantage Thus, it might refuse to accept imports of goods which were temporarily being dumped by other countries (that is, goods which were being sold to the socialistic country at prices lower than those prevailing for the same goods in the country

<sup>4</sup> Survey of Current Business, February, 1947, p. 42

of origin), unless such imports could be accepted without upsetting conditions at home. In deciding on imports and exports, a socialistic economy would attempt to take social costs, as well as money costs, into consideration. That is, in deciding to give up a particular industry at home and obtain its products by importation, the leaders would consider the problem of retraining the skilled labor formerly used in that industry and the benefits involved in getting rid of any bad effects which that industry had on its workers or which its soot, grime, and smoke had on the health of the citizens, or on their laundry and house-painting expenses.

*National Economic Self-Sufficiency* There is nothing about the program of ideal socialism to indicate that a socialistic economy would necessarily follow a policy of national economic self-sufficiency. If it were decided that certain commodities could be produced at home more cheaply than they could be imported in the long run, even though it were temporarily cheaper to import them, a socialistic economy probably would not hesitate to protect its "infant industries" by any necessary means. Again, if a socialistic economy found it necessary to operate as best it could in the midst of a generally hostile world, it might hesitate to depend too heavily on unfriendly countries for supplies of vital commodities and might undertake to produce such goods at home, even under relatively unfavorable cost conditions, in order to be economically independent. However, in a world composed of friendly socialistic economies, it would not be surprising if each economy relied on international trade to something like the extent implied as desirable by the Law of Comparative Advantage.

*The Trading Mechanism* In order to insulate the domestic socialistic economy from unplanned and undesired international influences to as great an extent as possible, all international trading would probably be done by a governmental monopoly created for the purpose. Individual enterprises and industries could dispose of their products abroad only through and with the approval of this governmental agency, and the same procedure would apply to the importation of goods desired by the consumers. The trading agency would work in close cooperation with the general agency for economic planning, and it would be expected to consider the general welfare rather than the private desires of individual citizens in making decisions with regard to importing and exporting. On occasion, the trading agency might decide to export quantities of

goods, which were badly needed by domestic consumers, in order to be able to import new machines or vital materials which were even more necessary from the point of view of the economy as a whole. In fact, the trading agency could disregard the costs of production at which its exports had been produced at home and sell the goods abroad at any prices which were not so low as to run afoul of the anti-dumping regulations of other countries, in order to be able to purchase desired imports. And it could pay almost any necessary price for such imports.

Further insulation of the domestic economy against international influences would probably be achieved by using separate currencies for domestic and international transactions, making any necessary conversions between the two currencies to meet the needs of travellers and persons desiring to make approved individual remittances between countries. Thus, either the trading agency or the central bank would have a complete monopoly of foreign-exchange transactions, and the value of the currency to be used for international purposes could be determined largely on the basis of expediency. Short-term movements of capital funds, as necessary for the financing of trade, would also be controlled by the government, but there is some doubt as to whether long-term capital movements would be permitted. In theory, it would be advantageous for a socialistic economy to borrow abroad until the arbitrary internal rate of interest had to be dropped to the level prevailing in other countries, or to lend until the planners found it necessary to raise the internal rate of interest to the level prevailing abroad. However, foreign borrowing would make the socialistic economy somewhat dependent upon other countries for economic goods, and foreign lending or investments would make the socialistic nation (according to the socialist point of view) into an indirect exploiter of the workers of other countries, so these long-term capital transactions might be avoided altogether.

*Foreign Trade under Communism* The theory of communism makes no apparent provision for international trade. It is difficult to see just how importing and exporting could be carried on between a communistic economy which operated without prices or money costs and another economy which operated on the basis of money prices and costs. Moreover, the presumed absence of government under full communism seems to preclude the possibility of trading through a governmental monopoly. Goods might be exchanged be-

tween two or more communistic economies on a basis of direct barter, but such trade would be rather difficult to arrange. On the whole, then, the prospects for international trade under communism do not seem bright.

### *The International Trade of Soviet Russia*

**The Trading Mechanism.** Since early 1918, international trade has been monopolized by the federal government of Russia, and this trade monopoly is now provided for by Article 14 of the federal constitution. A special Ministry of Foreign Trade, created for the purpose, has general responsibility for all import and export transactions. Neither private individuals nor governmental enterprises may enter into international transactions except through this Ministry and its agencies. The Ministry formulates the economic plans for foreign trade, which must be closely correlated with the general economic plans of the country, and sees that they are carried out through its branches, its trade missions to various countries, and its export and import corporations which specialize in particular types of goods.

The Ministry administers the customs laws and provides for the transportation of merchandise by sea in ships which it owns or hires. It also controls the prices of import and export commodities. In the case of exports, its control is complete, and the prices at which it sells goods in foreign markets may not be nearly the same as those that are paid to Russian enterprises and producers for the goods. In the case of imports, the Ministry cannot control completely the prices at which it purchases goods in foreign markets, but it does control the prices of imported goods within the Russian economy.

Through the state monopoly of foreign trade, Soviet Russia maintains strict and detailed control over imports and exports, obtains complete protection against the competition of other countries and against the possible upsetting influence of world market prices on the Russian domestic market, and is able to use its trade with other countries to pursue political and social ends as well as purely economic ones. Again, the state monopoly eliminates the need for the Russian internal currency to be linked to the foreign currency. The Russian ruble, as used in domestic trade, is not officially quoted in foreign markets, and fluctuations in the internal purchasing power of the ruble are not represented accurately by the official

rate of exchange. In establishing and maintaining an artificial value for the ruble for purposes of international transactions, the government prohibited the import and export of the rubles used within the country and the exchange of such rubles for foreign currency.

*The Development of Russian Trade.* In 1913, the total volume of Russia's trade with other countries amounted to 12.6 billion rubles, or about 3.8 per cent of total world trade. Exports amounted to about 6 per cent of domestic production, and imports to about 7 per cent. The exports included primarily grain, lumber, furs, hides, and other raw or partly processed goods, while imports consisted of finished manufactured goods, machinery and technical equipment, and industrial materials. After the revolution, Russian foreign trade virtually collapsed and in 1919-20 was running at about one-eighthieth of prewar levels. In 1922, foreign trade began to revive and it reached its highest level under the Soviet regime to date in 1930, in the middle of the First Five-Year Plan. In that year, exports amounted to 4.5 billion rubles and imports to 4.6 billion rubles, while the total volume of trade was at 73 per cent of that which had prevailed before World War I.<sup>4</sup>

Under the First Five-Year Plan, Russian foreign trade reached a fairly large volume because of the great program of industrialization which Russia was undertaking. Her needs for machinery, precision instruments, other industrial equipment, and certain industrial raw materials were great, and she proceeded to satisfy them by any means which lay ready to hand. Russian exports were based almost entirely on the desire to acquire foreign purchasing power, and any goods were exported which promised to have a ready sale in foreign markets, regardless of whether domestic supplies of these goods were relatively adequate or inadequate. Grain production was at low ebb in these years and near famine conditions prevailed in some years, but Russian grain exports averaged 453 million rubles annually from 1929 to 1932. The production of cotton textiles even by 1932 amounted to only a little over one-half the planned output, but exports of cotton textiles averaged 204 million rubles annually from 1929 to 1932.<sup>5</sup>

Since the Russian economy needed greatly to export, but it found that the exporters of other countries were rather firmly entrenched

<sup>4</sup> These statistics are from A. Yugow, *Russia's Economic Front for War and Peace*, pp. 98-100.

<sup>5</sup> *Ibid.*, p. 101.

in world markets and that many Russian goods could not yet compete with those of other countries on the basis of quality, there seemed to be no alternative except to secure foreign markets by charging extremely low prices for Russian exports. The prices charged were not only low in relation to those prevailing in world markets but were frequently below cost of production in Russia. In fact, one critic alleges that it was considered a brilliant accomplishment to obtain prices for exports of Russian cotton textiles which would cover 20 to 25 per cent of the costs of the enterprises which produced the goods, and that more commonly the price would cover only about 15 per cent of the costs.<sup>6</sup> This "dumping" of Russian products in foreign markets caused a great deal of irritation in other countries. The foreign exchange acquired by exportation was used to purchase the various materials necessary for rapid industrialization. In spite of great domestic shortages of consumers' goods of all kinds, imports of these goods made up only 10.2 per cent of all imports from 1929 to 1932, while 89.8 per cent consisted of goods for use in industry.<sup>7</sup>

During the Second Five-Year Plan, 1933-37, Russia became able to supply more of her own needs for industrial materials and equipment, and she reduced greatly or even discontinued imports of, for example, automobiles, tractors, electrical equipment, agricultural machinery, machine tools, iron and steel, cotton, wool, and paper. With the pressure to import somewhat lessened, Russia seems to have followed a deliberate policy of holding down the total volume of foreign trade. The announced policy is to limit exports to "surplus products of the national economy," and to restrict imports to whatever level is reached by exports. In 1938, the total volume of foreign trade amounted to only 23.9 per cent of that which had prevailed before World War I.<sup>8</sup> However, the composition of Russian imports had not changed greatly by 1938. While imports were very low, they still consisted largely (87.9 per cent) of goods for use in industry rather than of consumers' goods. On the other hand, the composition of Russian exports had changed greatly since the beginning of the First Five-Year Plan and since the years before the World War I. In the period 1909-13, agricultural products made up 70.6 per cent of Russian exports, and industrial products only

<sup>6</sup> F. Utley, *The Dream We Lost*, p. 234.

<sup>7</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 104.

<sup>8</sup> *Ibid.*, p. 100.

29.4 per cent Industrial goods exported in relation to total exports increased to 41.3 per cent in the period from 1922 to 1927, 61.3 per cent in the period from 1929 to 1933, and 72.8 per cent in the period from 1933 to 1937, while agricultural exports fell to 58.7, 38.7, and 27.2 per cent of the total in the same three periods.<sup>9</sup>

*Russian Trade in the War and Postwar Periods.* When World War II broke out, Russia began to purchase and stock-pile large quantities of a number of materials which would be indispensable if she became involved in the conflict. After being attacked by Germany, Russia had very little foreign trade in the ordinary commercial sense of the term, but she received large quantities of goods from her allies and was able to furnish them with more limited amounts of commodities and services in return. Russia received over 11 billion dollars' worth of aid from the United States, under the lend-lease program, from 1941 through 1946.

In the first three years after the end of the war, Soviet Russia was apparently trying to get as much economic assistance as possible from other countries while exporting the minimum amount of its domestic resources. The exports which have been made on a commercial basis have consisted largely of raw materials such as cotton, wool, flax, furs and skins, and coal. Other exports, including especially foods, have been sent on a political basis to such areas as Germany, Austria, Czechoslovakia, Rumania, and France in the hope of adding to the prestige and strength of the Communist Party in these lands. Russian exports, on the whole, have not been great enough to finance the importation of desired volumes of commodities, and Russia has been anxious to secure foreign credits to finance her purchases abroad. A long-term credit of \$250,000,000 payable in thirty years with interest at 2½ per cent was obtained from the United States to permit Russia to buy lend-lease goods which were "in the pipeline" (in process of manufacture or in transit) when lend-lease operations came to an end, and additional loans have been secured from other countries.

Soviet Russia has also acquired large quantities of goods from other countries by means of "non-commercial" methods. The Russian army in occupied lands has lived off the country, seizing the commodities it has needed. In addition, Russia has stripped occupied territories of industrial and agricultural machinery, railroad locomotives and cars, livestock, and other items. These acquisitions

<sup>9</sup> *Ibid.*, p. 102.

have been justified as representing the restitution of property taken from Russia during the war, as war booty to which Russia was entitled by right of conquest, or as reparations granted to Russia under the Potsdam Agreement.

Finally, Russia has obtained large quantities of goods from other countries through her ownership of enterprises and assets remaining in these areas. Former German assets in Rumania, Hungary, and Finland have been used as capital for investment in new joint Soviet-Rumanian, Soviet-Hungarian, and Soviet-Finnish enterprises. Although partly owned by the other countries, the enterprises are managed by Russian citizens who see to it that their output is thoroughly coordinated with the economic plans for the Russian domestic economy. In the Soviet zone of Germany the output of numerous enterprises seized by the Russians goes entirely to meet the needs of the Russian planned economy. In combination with other concessions granted by several countries, these developments give Russia the lion's share of the goods sent out of many of the countries of eastern Europe.

In trading with other countries since the war, Russia has favored the development of bilateral agreements which commonly provide that Russia's exports to and imports from the other countries shall be equal in value in each year or other specified period of time. Bilateral agreements have been concluded with Sweden, Yugoslavia, Bulgaria, Poland, Denmark, Rumania, Hungary, and other countries. The terms of such agreements can be kept relatively secret; they enable pressure to be brought to bear to secure price and other concessions from smaller and weaker countries, and the imports and exports which occur under them can be readily meshed with the general economic plans of Soviet Russia.

*National Economic Self-Sufficiency.* Disregarding the goods which were taken from Soviet Russia by noncommercial methods during the war or which she has secured by similar methods in the postwar period, it is possible to say that her foreign trade has been completely subordinated to the objectives of the national economic plans. It has been merely a tool for attaining the general goals of the economy. Soviet Russia has not attempted to import all goods which could be produced more cheaply in other countries than at home or to export only those goods which could be produced more cheaply in Russia than in other countries. Strict adherence to this policy might have caused Russia to remain a backward agricultural



ber-bearing plants which she discovered rather than to the manufacture of artificial rubber from petroleum or alcohol. However, if Russia abstained for the most part from the production of synthetic materials, this result was due probably to the fact that her great variety of climatic conditions and natural resources made it possible to produce most kinds of goods by natural methods, rather than to any unwillingness on her part to produce synthetic materials if necessary. Russia also achieved a high degree of economic self-sufficiency without maintaining high protective tariffs, import quotas, and other devices which play a conspicuous part in the policies of other countries, but her governmental monopoly of foreign trade furnished a much more powerful means of control than any of these other things.

While Russia's great variety of climatic conditions, and natural resources made it possible for her to achieve a high degree of economic self-sufficiency, we should not assume that she was able to attain this goal at no cost to herself, for the Law of Comparative Advantage applies to Soviet Russia as well as to any other country. Some kinds of goods can be produced in Russia only with considerable difficulty and, even if all types of goods could be produced there readily, Russia would still find that she could produce some goods with greater relative efficiency and lower cost than others. Every country, whether under a socialistic or capitalistic régime or any other variety and whether her natural resources are many and varied or few and limited, can gain in terms of standards of living by concentrating her productive energies on those lines of production in which she can develop the greatest efficiency and lowest cost, while obtaining the products of other industries by means of foreign trade. Russia was able to obtain a great degree of economic self-sufficiency only at the cost of furnishing her citizens with standards of living lower than those which could have been attained on the basis of geographical specialization and international trade.

Now, of course, it is probable that the Russian leaders were under no illusions in following a policy of economic self-sufficiency. Their aims did not include high immediate standards of living for the consumers of the country, but rather rapid industrialization and general economic development. The policy of economic self-sufficiency was dictated to a large extent by the fact that Russia's economic development had to take place in the midst of a relatively

hostile nonsocialistic world and the fact that Russia considered herself to be living in constant danger of attack by some other country or countries. Self-sufficiency meant preparedness for war, and the degree of it which Russia attained was found to be very useful during World War II.

### QUESTIONS

- 1 "Differences in the endowment of productive agents between countries may be either absolute or comparative." Explain
- 2 "It is economically advisable for a country to produce all types of economic goods which it can produce with greater efficiency than other countries." Show whether you agree
- 3 What are the leading effects of international trade on the various trading countries?
- 4 How and why do the governments of capitalistic countries often interfere with the course of international trade? Explain
- 5 "The United States, like many other capitalistic countries, has followed a policy of restrictionism with respect to international trade for many years" Explain
- 6 "After the outbreak of World War II, the government of the United States imposed many new restrictions and controls on international trade" Explain
- 7 "The international trade of the United States declined sharply during World War II under the influence of severe governmental controls. Do you agree? Explain
- 8 "Since the Law of Comparative Advantage would apply to a socialistic economy, such an economy would be committed to a policy of complete free trade" Show whether you agree
- 9 In view of the arbitrary character of the costs of production under socialism, how could a socialistic economy decide on the relative cheapness of imported and domestic products?
- 10 There is nothing about the program of ideal socialism to indicate that a socialistic economy would necessarily follow a policy of national economic self sufficiency" Do you agree? Explain
- 11 How could a socialistic economy insulate itself against unplanned and undesired international influences?
- 12 "It is difficult to see how international trade could be carried on between a fully communistic economy and economies of other types" Explain
- 13 How is international trade carried on by the socialized economy of Soviet Russia? Explain
- 14 What is the Soviet Russian policy with respect to international trade?
- 15 "The trading policies of Soviet Russia have sometimes been disturbing to other countries" Explain

- 16 "Since Russia went to war in 1941, her foreign trade has been largely on a non-commercial basis" Explain
- 17 Describe the leading developments in the foreign trade of Soviet Russia in the first few years after World War II
- 18 Which of Russia's policies with regard to foreign trade have been inherent in the nature of a planned economy, and which have been inspired by the peculiarities of Russia's situation? Explain
- 19 "Soviet Russia has made no attempt to follow a policy of national economic self-sufficiency" Show whether you agree
- 20 "The costs of national economic self-sufficiency for Soviet Russia have probably not been very great" Explain

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## CHAPTER 20

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### **INTERNATIONAL TRADE**

*(Continued)*

#### *The International Trade of Britain under Partial Socialism*

**The Prewar Situation in British Trade** For many years, Britain has had to buy very large quantities of food and raw materials (and some manufactured goods) from other countries each year in order to exist and produce. Before World War II, her merchandise exports quite regularly failed to pay for her merchandise imports, but the deficit in each year was eliminated, or at least reduced to manageable proportions, by the income received from other countries on her foreign investments and that obtained by selling services, such as shipping and insurance. In 1938, for example, her imports amounted to £835,000,000 and her exports and re-exports to £533,000,000, leaving an adverse balance of £302,000,000, but a net income of £232,000,000 with respect to the so called invisible items of trade left her with a net overall deficit of only £70,000,000.<sup>1</sup>

**The Postwar Crisis** The British situation with respect to international trade was very different when the Labor Government took over and World War II came to an end. Wartime destruction in Britain had reduced the country's ability to produce and export, while large-scale imports were most essential. During the war, Britain had lost a major part of her shipping (some three billion dollars' worth), had had to sell capital assets abroad valued at  $4\frac{1}{2}$  billion dollars, and had incurred new foreign liabilities amounting to  $11\frac{1}{2}$  billion dollars. Her net income from the invisible items of trade had been changed to a net deficit, and there seemed to be no way to pay for her excess of merchandise imports.

<sup>1</sup> *Labor and Industry in Britain*, March, 1948, p. 3

Britain's imports in 1946 amounted to £1,092,000,000, and her exports to £888,000,000 leaving an adverse balance of only £204,000,000 with respect to merchandise, but the invisible items produced a net outgo of £176,000,000 instead of a net income and listed the net overall deficit to £380,000,000.<sup>2</sup> This unfavorable result had come about in spite of strenuous efforts to increase production and exports and to cut imports to the bone, and Britain was able to keep on going only by securing large loans, amounting to \$5,000,000,000 altogether, from the United States and Canada. These credits were supposed to take care of temporary deficits in Britain's balance of payments and tide her over until she could get back on her feet again.

In 1947, however, the situation went from bad to worse. Although Britain's imports in 1947 were only 76 per cent of those of 1938 by volume, while her exports were 108 per cent of those of 1938 by volume, her adverse balance with respect to merchandise trade increased from £204,000,000 to £449,000,000.<sup>3</sup> This happened because the prices of goods imported by Britain increased much more rapidly than those of her exports. In the third quarter of 1947, the prices of Britain's exports were 126 per cent higher than in 1938 and the prices of her imports were 167 per cent higher than in 1938.<sup>4</sup> Even a parallel increase in the prices of imported and exported goods would have increased her trade deficit, since her imports regularly run larger than her exports, and the more rapid increase in the prices of imported goods was particularly devastating.

Britain's net income from foreign investments and shipping came to only £68,000,000 in 1947, while governmental expenditures overseas amounted to £211,000,000, and the net outgo on account of other invisible items was £83,000,000. The net deficit of £226,000,000 in connection with the invisible items of trade, coupled with that of £449,000,000 in connection with ordinary imports and exports, brought the net overall deficit to £675,000,000.<sup>5</sup> This large deficit was entirely with the Western Hemisphere and could therefore be correctly expressed in dollars—\$2,700,000,000. In fact, Britain's deficit with respect to the Western Hemisphere was £680,-

<sup>2</sup> *Ibid*

<sup>4</sup> *Ibid*, p. 4

<sup>3</sup> *Ibid*, p. 6

<sup>5</sup> *Ibid*, p. 3

000,000, but a slight surplus of £3,000,000 with the rest of the world brought the net figure to £675,000,000.<sup>6</sup>

A part of Britain's difficulties in 1917 was caused by the fact that she had to pay out large quantities of dollars for other countries. As a condition of obtaining the large loan from the United States in 1916, Britain had agreed to make her currency fully convertible for current transactions by July 15, 1917. This meant, broadly speaking, that other countries selling goods or services to Britain could convert the pounds sterling they earned into any other currency, including dollars. The world demand for dollars in 1917 proved to be too great to permit this experiment to be successful. Other countries began converting into dollars all the sterling they could get their hands on, and not merely their surplus sterling, and the drain on Britain's dollar credits was so excessive that sterling convertibility had to be suspended on August 20, 1917.

*Solving Britain's Trade Problem* In the last few months of 1917, Britain's Labor Government took drastic steps to bring about a solution of the country's problems with respect to international trade and the balance of payments. Further immediate reductions in imports were announced, and the domestic rationing program was made more severe than before. Since a large part of Britain's imports consisted of raw materials which helped to manufacture exports and hence could not be curtailed, the reduction of total imports had to bear very heavily on imports of food and consumers' goods. A second part of the program was to save on imports by obtaining increased supplies of some goods from domestic sources. This part of the program was typified by the large-scale plan to develop home agriculture which was set in motion in the fall of 1917.

A third item was a general cut in Britain's program for domestic capital investment and also a rearrangement of its parts. The object was, of course, to cut down investments which would require the use of large quantities of materials that had to be imported and paid for with dollars and to concentrate investments where they would do the most immediate good in connection with increasing production and exports. In the fourth place, the British government's controls over manpower, materials, and other factors were to be used to achieve the greatest possible increase in total exports. Finally, Britain's foreign trade was to be rearranged so as to im-

<sup>6</sup> *Ibid.*, p. 6

prove her position with respect to the Western Hemisphere. Every thing possible was to be done to increase the production and export of goods which could be sold in the United States, Canada, the Argentine, and other hard currency markets, even at the expense of exports to some other countries from which Britain's needs were less urgent. Attempts were made to create new sources of supply for British imports in countries outside the Western Hemisphere where payments could be more readily made. Other Sterling Area countries were invited to exercise similar measures of economy in the use of dollars and to stimulate exports to dollar-earning destinations.

As a result of all these measures, British exports were supposed to be running at 154 per cent of the 1938 level by volume at the end of 1948, while in the matter of imports the line was to be rigidly held. In financial terms, imports for 1948 were to amount to £1,670,000,000 and exports and re-exports to £1,500,000,000, thus reducing the adverse balance with respect to merchandise to £170,000,000, as compared with £449,000,000 in 1947. Cuts in governmental expenditures overseas, reductions in expenditures for foreign travel and motion picture films, and the rebuilding of the shipping fleet were to reduce the deficit in connection with the invisible items from £226,000,000 in 1947 to £80,000,000 in 1948. Thus the net overall deficit in Britain's balance of payments was to be cut from £675,000,000 in 1947 to £250,000,000 in 1948.<sup>7</sup> These results would have been helpful, if achieved, but they would have left Britain's deficit in the balance of payments at about one billion dollars in 1948, so there was little doubt that Britain was glad to see the Marshall Plan, involving further large amounts of assistance from the United States, go into effect in the first half of the year. It was impossible to predict when Britain's crisis with respect to international trade and the balance of payments would finally be over.

### *International Trade under Fascism*

The record of the international trade of Italy and Germany under fascism was much the same as that of other phases of economic life. That is, the actual business of importing and exporting was left to a considerable extent in the hands of private individuals and firms, but it was subjected to ever increasing governmental control.

<sup>7</sup> *Economic Survey for 1948*, pp. 8-14.

In the period of economic recovery and prosperity after 1922, Italy's international trade expanded considerably. In 1922, Italy's exports amounted to 9.6 billion lire and her imports to over 11 billion lire. By 1928, exports had increased to 14.6 billion lire and imports to 21.9 billion lire.<sup>8</sup> In all these years, Italy had a so called unfavorable balance of trade, with imports of merchandise exceeding exports by a relatively large amount. This result was not surprising, in the light of the theory of international trade, for Italy's exports were largely nonessential goods, such as fruits and vegetables, cheese, fine textiles, and other specialties, while her imports consisted largely of vital materials and foods, such as coal, oil, woodpulp, cotton, wool, grains, and iron and other metals.

However, the unfavorable balance of trade with respect to commodities was not a source of great embarrassment to Italy, for her invisible exports normally exceeded her invisible imports by enough to pay for her surplus of merchandise imports. The most important of these invisible exports were emigrants' remittances, tourists' expenditures in Italy, and payments for freight and shipping services. Emigrants' remittances had been as great as 5 billion lire in some years, and in 1924 Italy had received 1,060,000 foreign tourists who spent 2.9 billion lire.<sup>9</sup> Even in 1929, the three main invisible exports brought in a net balance of well over 5 billion lire.<sup>10</sup> These receipts from invisible exports gave Italy a balance of foreign purchasing power with which to pay for commodity imports.

*Experiences in the Great Depression.* Italy's foreign trade was already on the down grade by 1929. The currency stabilization of December, 1927, which placed the lira at a relatively high value in terms of foreign currencies, brought difficulties for foreign trade. Italy's prices appeared high in terms of foreign currencies, and her exports began to decline, while imports had to be rather well maintained. The Italian government attempted to restore some sort of equilibrium by decreeing successive reductions in prices, wages, and costs in general, but before any real relief could be obtained Italy, like other countries, was hard hit by the great post-1929 depression. Italian imports fell from 21.9 billion lire in 1928 to 7.7 billion lire in 1934, and her exports declined from 14.6 to 5.2 billion lire over the same period.<sup>11</sup> In spite of the great decline in both imports and

<sup>8</sup> W. G. Weil, *Fascist Economic Policy*, p. 204.

<sup>9</sup> W. Ebenstein, *Fascist Italy*, pp. 190-191.

<sup>10</sup> W. G. Weil, *Fascist Economic Policy*, p. 205.

<sup>11</sup> *Ibid.*, p. 204.

exports, a rather large unfavorable balance of trade with respect to commodities still remained, and it was no longer being offset by a surplus of invisible exports. From 1929 to 1932, the surplus of invisible exports declined from 5.4 to 2.2 billion lire.<sup>12</sup> Even in 1931, commodity exports had paid for 88 per cent of commodity imports, but this percentage declined to 68 by 1934.<sup>13</sup> In this situation, frequent outflows of gold occurred, and great pressure was brought to bear on the foreign-exchange markets and gold reserves of the country. Increased governmental control over trade seemed very necessary.

Germany's difficulties in connection with international trade and foreign exchange began in earnest in 1929, some four years before the National Socialist Party came into power. In the great depression which began in 1929, German exports fell off sharply and invisible net payments to Germany on account of tourist expenditures and shipping, insurance, and banking services declined greatly. On the other hand many German imports of vital foods and raw materials had to continue even in depression years and Germany was still supposed to make reparations payments and pay interest and principal on her other debts. Foreign trade had been extremely important to Germany since she established herself as an industrial economy. Even in 1931, a year of depression, Germany exported 36 per cent of her entire industrial production and depended on other countries for 40 to 45 per cent of her raw materials. In 1934, 58 per cent of German imports were raw materials. Her dependency on foreign materials amounted to 100 per cent for the cotton, jute, rubber, and silk industries, 60 per cent for the leather industry and heavy industries in general, and 35 per cent for the margarine, beer, and tobacco industries. Germany imported 90 per cent of her wool, 95 per cent of her flax, 32 per cent of her motor fuels in general, and 80 per cent of her gasoline.

The unfavorable turn taken by her imports and exports in the great depression was a matter of serious concern to Germany. The Reichsbank's holdings of gold and foreign currencies, which had amounted to 2284 million marks at the beginning of 1929, declined to 920 million marks at the end of 1932, 449 million marks in May, 1933, and 136 million marks in May, 1934. The Hoover moratorium of 1931 and the end of reparations at Lausanne in 1932 afforded

<sup>12</sup> *Ibid.*, p. 205

<sup>13</sup> *Ibid.*, p. 206

only temporary relief, and the new National Socialist government, when it came into power in 1933, proceeded to intervene strongly in the field of international trade and foreign exchange.

*Import, Export, and Exchange Controls.* The controls imposed on international trade by the governments of the fascist countries were of many types. In Italy, imports were controlled in part by a licensing system. Individuals and firms were allowed to import certain specified commodities only if they had licenses issued by the Minister of Foreign Trade and Exchange, who was assisted in the work of licensing by an import advisory committee representing retailers, manufacturers, and labor. Comparatively few commodities were brought under the licensing system at first, but the number grew to about 1500 before the end of 1935. Commodities which did not come under the licensing system were subjected in many cases to import quotas under which, in general, imports in each year could amount to only 10 to 70 per cent of the amounts which were imported in 1934. However, imports up to 100 per cent of the 1934 amounts were permitted from countries with which Italy had concluded clearing agreements, so that trade involved no actual use of foreign exchange. Restricted imports were rationed within Italy through the category corporations, and allotments of goods to individuals and firms were based in general on their importations in 1934. Some commodities came to be imported exclusively by governmental monopolies.

Tariff duties were raised and Italy had one of the highest protective tariffs in existence by 1935, with duties ranging from 185 to 274 per cent higher than in 1914.<sup>14</sup> The Ministry of Foreign Trade and Exchange set up the National Foreign Exchange Institute and, as early as December, 1934, all Italian exporters were required by decree to sell to the Institute all foreign exchange which they received and all foreign credits which they were granted in connection with export transactions. The Institute would then allot foreign exchange in order that payments might be made for the ordinary variety of imports and for goods received under different kinds of trading agreements with various countries. Italy also strengthened her position with respect to foreign purchasing power by requiring individuals and firms to turn in foreign securities and other credits which they owned in exchange for bonds of the Italian government.

In Germany, payments of interest and principal on debts to for-

<sup>14</sup> C. T. Schmidt, *The Corporate State in Action*, p. 126.

eign countries were suspended almost as soon as the fascists came into power Instead of being transferred to the creditor countries, these payments were deposited in Germany in the form of blocked marks, which could be used for various purposes within the country and especially for financing exports, but could not be transferred in cash to other countries All exporters were soon required to register all sales abroad with the Reich Foreign Exchange Board and the Administration of Self-Help of German Industry (or Export Subsidy Fund) Prices of exported goods were strictly controlled and all foreign exchange received from exports had to be sold to the government, which would then ration it out to permit necessary imports

At first importers were allowed to buy annually 75 per cent of the amount of foreign exchange which they had used in the base period from June, 1930 to July, 1931, but the allotment was cut by a third by May, 1934, and was placed on a day-to-day basis, dependent on the Reichsbank's receipts of foreign exchange, by the end of June, 1934 This system worked most unsatisfactorily, and a new plan was instituted in September, 1934, with the intention of holding imports strictly down to the amount of foreign exchange available, confining imports to countries which accepted equivalent quantities of German exports, and giving priority to certain imports of raw materials and especially those necessary to the armaments program Much of the control under the new plan was placed in the hands of the 27 import-control boards, or supervisory boards for imports, which were set up Only imports for which one of these boards had issued permits could enter the country The issuance of permits depended on the importance of the prospective imported goods, their prices, the availability of foreign exchange, and other matters When the time arrived to make payments for imports, importers who could prove that the goods had actually been imported could obtain foreign exchange from the Reichsbank up to the amount specified by the permits which they had received The foreign exporters eventually received drafts of the usual sort After 1939, the control powers with respect to imports were apparently in the hands of some 31 Reichsstellen, or agencies for the rationing of raw materials, which were under the supervision of the Ministry of Economic Affairs Through these agencies, imported and domestic raw materials were handled together and were apportioned among firms and industries in accordance with the needs of the war economy

Although these various devices were successful in stabilizing the foreign trade and balance of payments of the fascist countries, they gave a great deal of difficulty in other respects Large numbers of officials were required to administer them, and they operated to discriminate in favor of the larger firms, which were better known, had more influence with the controlling agencies, and could finance the necessary time-consuming negotiations The controls involved fascist importers and industrial firms in much extra expense and inconvenience As one writer on Germany said, "At least half the time of a German manufacturer is spent on the problem of how to get scarce raw materials These cannot be obtained without a certificate from one of the supervisory boards which distribute the available raw materials, domestic as well as foreign Usually a manufacturer needs dozens of different materials He cannot work without any one of them For each one there is a special supervisory board with a different procedure, with all of which the business man must be familiar "<sup>15</sup> Since fascist enterprises always wanted greater quantities of imported and other materials than were available, a system of priorities was developed to make sure that the limited quantities of materials would satisfy the most urgent needs However, upon occasion, urgency certificates were issued for greater quantities of materials than were available The problem of allocating limited quantities of imported and other materials among industries, and among firms within industries, was a trying one

*Governmental Trading Agreements* The governments of the fascist countries negotiated trading agreements with the governments of many other countries Sometimes these were "payments agreements" under which the total amounts of foreign exchange received from exports and used to pay for imports were balanced, and sometimes they were "clearing agreements" under which the total values of goods imported and exported were balanced Under agreements of the latter type, trade took place on a straight barter basis and supplies of foreign exchange were not required The German government was a past master in the use of these barter agreements

The German government would get other countries to send foods or raw materials to Germany and would offer to pay prices well above the world level for these goods The prices were paid in various kinds of blocked marks, which could be used only to pay

<sup>15</sup> G. Reimann, *The Vampire Economy*, p. 52 Reprinted by permission of The Vanguard Press, New York

for German exports. Germany was then supposed to export manufactured goods to the other countries to complete the transactions. In the early stages of such transactions, Germany would accept almost any available surpluses of foods or raw materials and would give the other countries manufactured goods which they actually needed. Later on, and especially when the other countries had piled up large balances of blocked marks in Germany, the other countries were made to furnish exactly the foods and raw materials which Germany wanted and to take almost any goods which Germany could spare in exchange. Some small countries were made to adjust their economic systems almost completely to German requirements, and even give Germany a voice in the management of their enterprises.

Germany would not furnish goods which could be sold directly in other countries to obtain foreign exchange, goods which were scarce in Germany, or goods made largely of foreign materials. She would give the other countries a choice of receiving nothing at all or of taking any products of which Germany had a surplus. In this way, Germany developed a host of unsatisfied customers. Thousands of typewriters were sent to Rumania, machinery-needed Turkey was given a bumper supply of coffee mills, gramaphones, and radios, the peasants of Bulgaria and Yugoslavia were regaled with field glasses and optical instruments, and the warehouses of Mexico were made to groan with their load of barber chairs. Even the Standard Oil Company of New Jersey sent some oil to Germany and received in return enough mouth organs (harmonicas) to give each boy in the United States at least two. While some South American countries, which sent foods or raw materials to Germany, were undoubtedly surprised to receive shiploads of aspirin in return, they at least must have found this import practical, as would any other country which engaged in barter trade with Nazi Germany. The unpopularity of the barter deals was also increased upon occasion by Germany's practice of reselling certain barter imports (such as coffee) on the world markets—a practice that often worked to the disadvantage of the countries which had furnished the barter imports.

*Private Trading Arrangements.* The German government under fascism also sponsored a number of types of private trading arrangements which amounted substantially to barter. Under one kind of private arrangement, a German importer who desired to obtain goods from the United States would seek a German exporter who was unable to sell his goods in the United States because his price,

at the nominal rate of exchange, was too high. The importer would pay the exporter a premium that would make it possible for the exporter to sell his goods in the United States at the price obtainable there. The sale would create exchange with which the importer could obtain the goods which he desired and he would recover the premium paid to the exporter by selling the imported goods at a high price in Germany.

Many private trade transactions were financed by the famous Aski marks, which could be used only to pay for German exports. A German importer would make an offer to import goods from some foreign firm and pay for them in Aski marks. The foreign exporter, knowing that the Aski marks could be sold only at a considerable discount, would charge the German importer a high price in terms of these marks. The foreign exporter would get the net price which he desired by selling the Aski marks at a discount to an importer in his country. The foreign importer, since he had obtained the Aski marks so cheaply, could then afford to buy German exports at the high prices prevailing in Germany. Since they did not place any strain on the German supply of foreign exchange, international transactions involving Aski marks did not originally come under the foreign exchange control and the import-control boards. However, these transactions eventually grew unwieldy; goods of an undesired luxury or semi-luxury character were imported by means of these transactions, and goods were exported on the basis of Aski marks that could have been sold directly in foreign countries to obtain foreign exchange. As a result, imports on the basis of Aski marks were brought under the jurisdiction of the import-control boards and, in 1935, many goods were excluded from transactions involving these marks. The transactions of this kind were eliminated entirely in 1937.

*Export Subsidies* Both fascist countries operated systems of subsidies for the benefit of exporters. In Germany, for example, exporters were required by the government to charge high prices in markets in which no competition existed, but in other markets the exporters needed to be able to dump goods freely at low prices. This power was furnished through the Administration of Self-Help of German Industry, or Export Subsidy Fund. The funds for export subsidies were furnished in part by the German government and in part by German industries. The Estate of Industry and Trade collected the funds furnished by German industries and determined

the size of their contributions. It was reported that, in 1938, the industries contributed 1200 million marks, while the government chipped in with 500 million marks.<sup>18</sup> The funds were used to pay subsidies, ranging up to 40 to 45 per cent of sales prices in Germany, to German exporters who sold their goods abroad at prices which would cover only a part of the costs of producing the goods. German exporters were also sometimes subsidized in effect by being allowed to spend a part of the foreign purchasing power, which they acquired, for imports which could be sold at highly profitable prices in Germany, or by being given highly profitable prices for such parts of their output as were sold at home, and especially if sales were made to the German government.

*Principles and Results of Fascist Trade Policy.* In the period from 1933 to the beginning of World War II, the objective of fascist trade policy was to satisfy the domestic demand for imports as a necessary supplement to home production and an aid in preparing for war, and not to achieve the maximum possible volume of exports or to exploit every opportunity for foreign trade which seemed to be advantageous from the point of view of profits. While Italy devalued the lira by 40.94 per cent late in 1936, German trade policy involved the use of many kinds of marks of different values. An open devaluation of the German mark might have brought gains in trade, but it would have meant treating all other countries equally well (or equally poorly). The use of many kinds of marks of different values enabled Germany to treat each country as well as necessary, but no better.

In carrying on international trade, the fascists made a practice of respecting the property rights of foreign countries, individuals, and firms only when these rights could be protected by absolute power or direct retaliation. Under ordinary conditions fascist buyers would cancel orders freely, sellers would fail to fill orders, and so on. The foreign victims might in some cases fight and win court cases in the fascist countries, but no transfers of funds abroad to pay damages would be permitted in any case. Fascist firms having assets abroad which made them vulnerable to the decisions of foreign courts had to behave more circumspectly, and fascist firms in general were required to be very kind in their dealings with foreign countries with respect to which the balance of trade was favorable.

Under the various control measures which we have outlined, the

<sup>18</sup> *Ibid.*, pp. 232-233.

fascist countries succeeded in stabilizing their trade and in keeping their imports and exports rather well balanced, but then total trade remained on a rather low level. In 1935, during the Ethiopian campaign, the League of Nations applied economic sanctions to Italy, and 32 countries suddenly stopped buying Italian commodities. Italy then used the restrictionary machinery, which had been set up already, to limit her imports further, both to protect her own balance of trade and to retaliate against the countries which had imposed sanctions. Italy's trade in 1936 was even below the depression levels. Exports amounted to 55 billion lire, imports to 60 billion lire, and the unfavorable balance to 500 million lire.<sup>17</sup> In 1937, after the Ethiopian war and the sanctions were over and under the influence of the devaluation of the lira, Italian trade picked up considerably. Exports were valued at 104 billion lire and imports at 138 billion lire, while the unfavorable balance amounted to 34 billion lire.<sup>18</sup>

Italy's foreign trade in 1938 was less than in 1937. Exports remained at approximately the 1937 level, but imports declined by almost 19 per cent. World War II began in 1939 and Italy's trade went from bad to worse. Especially after her entry into the war, Italy was cut off from her overseas markets and sources of supply, and was deprived of foreign purchasing power by the disappearance of emigrants' remittances, tourist expenditures, and payments for freight and shipping services. Trade went on only with neighboring countries, and Italy became more and more a mere satellite of Germany. Even in 1939, Germany furnished 26.5 per cent of Italian imports and received 24.6 per cent of Italian exports.<sup>19</sup> Italy depended on Germany for vital commodities, such as coal, machine tools, machines, non-ore and scrap, lumber, and oil, while Italy furnished only such commodities as fruits and vegetables, hemp, mercury, and sulphur.

War with Greece further lowered Italy's trade possibilities, and Italy had great difficulties in holding up her end of the trade with Germany. In October, 1940, there was a balance of 416 million lire in favor of Germany in the Italo-German clearing account, and Italy agreed to make payment by exporting workers to Germany.

<sup>17</sup> W. G. Weil, *Fascist Economic Policy*, p. 10.

<sup>18</sup> *Ibid.*

<sup>19</sup> *Foreign Commerce Weekly*, December 11, 1940, pp. 487 and 535.

whose wages could be balanced against Italy's surplus of imports.<sup>20</sup> A decree of January 13, 1941, provided for the requisition of Italian products for exploitation by the Italian government and of raw materials and semi-manufactured goods to be made into finished products for exportation.<sup>21</sup> In February, 1941, Italian payments of clearing debts to Germany were suspended. Germany agreed to continue to supply Italy with coal and war materials and to take fruits and vegetables and badly needed workers in return.<sup>22</sup> Such makeshift arrangements continued during the remainder of Italy's participation in the war.

German exports had fallen from 12.3 billion marks in 1928 to 4.17 billion marks in 1934, and her imports had declined from 14.0 to 4.45 billion marks over the same period.<sup>23</sup> In the period from 1934 through 1938, German exports varied only between 4.1 and 5.8 billion marks, imports varied only between 4.1 and 5.4 billion marks, and the net balance of trade ranged only from an export surplus of 500 million marks to an import surplus of 300 million marks.<sup>24</sup> German exports in relation to total industrial production declined from 22.5 per cent in 1933 to 13.1 per cent in 1938. In many cases it was apparently more profitable for German industries to produce armaments and other goods for the government than to turn out goods for export. In order to have enough foreign exchange to obtain necessary raw materials, it was necessary to curtail imports of food in this period, since foreign loans could not be obtained and since only about 20 per cent of all German exports were producing foreign exchange.

German trade slumped considerably after the outbreak of World War II, for overseas trade was almost completely eliminated. However, in late 1940 the Nazi leaders claimed that foreign trade had reached prewar levels. Losses due to the war had been offset by "trade" with the occupied countries and with Soviet Russia. However, trade with the occupied countries was on a noncommercial basis and meant merely that the Germans helped themselves to whatever they could lay their hands on. Such appropriations of wealth, while immediately profitable, could not go on indefinitely.

<sup>20</sup> *Foreign Commerce Weekly*, January 4, 1941, p. 15.

<sup>21</sup> *Foreign Commerce Weekly*, April 12, 1941, p. 70.

<sup>22</sup> *The Economist* (London), March 15, 1941, p. 16.

<sup>23</sup> M. T. Flounsky, *Fascism and National Socialism*, p. 208.

<sup>24</sup> Reichskreditgesellschaft, *Economic Conditions in Germany in the Middle of the Year 1939*, pp. 32-33.

in individual occupied countries, and their continuation depended upon additional conquests which eventually were not forthcoming.

*The Fascist Self-Sufficiency Programs* Since it was clear long before World War II began that the foreign trade of Germany and Italy, under fascist policies, was not likely to return to the levels of 1928 and 1929, and since thorough preparation for war seemed to require these countries to be as independent as possible of foreign sources of supply of vital raw materials and foods, both Germany and Italy undertook comprehensive programs for attaining national economic self sufficiency. In each country, the self sufficiency program included three related parts or phases.

In the first place, efforts were made to increase the production of articles which, though already produced in the fascist countries, were not being turned out in adequate amounts. This phase of the program was typified by the Italian Battle of the Wheat, which had begun some years earlier. In winning this battle, wheat cultivation was expanded so that one-sixth of the total land area of the country and one-fourth of the cultivated area was devoted to this crop. The yield of wheat per hectare of land was also increased moderately, though increases which were almost as great occurred in other European countries that had no battles of wheat, and Italian production per hectare ranked sixteenth among those of 28 European wheat-producing countries.<sup>25</sup> Italy's wheat production, which had amounted to an annual average of 53,904,000 quintals from 1921 to 1925, increased to one of 60,705,000 from 1926 to 1930, and 70,724,000 from 1931 to 1936.<sup>26</sup>

In German agriculture, farmers were asked to double the number of sheep raised for wool, to double also the quantity of land used for raising fibrous and oil-bearing plants, and to increase the production of flax sharply. Efforts were made to increase the supply of farming land by draining swamps and reclaiming meadow-land. In Italian industry, attempts were made to increase the production of coal, iron ore, aluminum, dyes, paper, and oil. Deposits of low-grade coal were brought into production and efforts were made to refine low grade crude oil from Albania and to obtain oil from the distillation of domestic lignites. In German industry, the program aimed at the increased production and use of domestic metals such as aluminum and magnesium and at establishing plants which would

<sup>25</sup> W. Ebenstein, *Fascist Italy*, pp. 198-199.

<sup>26</sup> *Ibid.*, p. 201.

make use of low-grade domestic deposits of iron ore, zinc, lead, and copper.

A second phase of the self-sufficiency programs involved attempts to substitute articles of which the fascist countries had relatively adequate supplies for other commodities which were relatively more scarce. In Italy, textiles of rayon and hemp were substituted for those made of wool and cotton, alcohol was mixed with gasoline for use as motor fuel, castor oil was used for the lubrication of machines and vehicles, cadmium was substituted for copper, and the railroads were electrified in order to make use of the relatively plentiful electric power instead of the relatively scarce coal.

In Germany, construction was carried on with more concrete and less steel, alloys and plastics were substituted for scarce metals in making some kinds of machinery, glass was used for pipes, insulation, and food containers in the place of metals. Paperboard containers also replaced those of metal and wood. Door handles, hinges, curtain rods, and other door and window hardware were made from wood instead of metal. Brake linings were made of steel or aluminum wool (rubberized with synthetic rubber). Gasoline was saved by running automobiles and busses on illuminating gas or generator wood gas. Leather for belts and handbags was made from rabbit skins, and shoes were produced with uppers of leather made from rabbit or fish skins and soles of wood. Aluminum was substituted for tin, zinc for brass and bronze, and copper for lead.

Finally, the program included the making of artificial or synthetic substitutes for a variety of natural products in connection with which shortages existed. Germany had been dependent on imports of cotton and wool to a great extent for many years, but, from 1929 to 1938, German imports of cotton fell 48 per cent in quantity and 77 per cent in value while those of wool fell 33 per cent in quantity and 72 per cent in value.<sup>27</sup> Besides increasing the production of artificial silk or rayon greatly, Germany learned to make textiles out of "cell wool," made from wood or skimmed milk. Though the production of cell wool increased from 5000 to 150,000 tons from 1933 to 1938, Germany in the latter year could produce only a little over 22 per cent of her requirements of textile raw materials.<sup>28</sup>

The production of synthetic gasoline from coal was developed, and Germany's ability to fill her ordinary peacetime requirements

<sup>27</sup> G. Reimann, *The Vampire Economy*, pp. 201-202.

<sup>28</sup> *Ibid.*

for oil increased considerably. That is, she could produce half enough oil at home in 1939, as compared with 20 per cent in 1935.<sup>20</sup> The production of synthetic rubber was increased to the point where it filled one-fourth of Germany's needs in 1938 and one-third in 1939, but imports in 1938 were still two thirds greater than in 1933.<sup>21</sup> These imports presumably were used in part for the accumulation of stock piles of the natural rubber. The production of "woodpulp" from straw reached 180 thousand metric tons in 1939, an increase of 109 thousand tons over 1936. An excellent butter, purer and better than natural butter, was made from coal tar. It was discovered that 32 pounds of cheap fish would yield one pound of extract which was said to equal 160 hens' eggs in food value. German authorities claimed to be able to save 400 million eggs per year through the use of these "Viking eggs."<sup>22</sup>

Artificial cinnamon was made from the powder of pulverized shells of hazelnuts or almonds, colored brown and treated with a mixture of 96 per cent cinnamic aldehyde, 4 per cent eugenol acid, and a trace of cinnamon oil for fragrance. In 1940, Germany announced the invention of a highly elastic mineral fiber, made from coal and lime, to replace iron in the construction of reinforced concrete. The new substance was said to be capable of production in almost limitless quantities, practically immune to decay, noninflammable, and unaffected by water.<sup>23</sup> Other substitutes included artificial bristles, soap made from coal, glass shoes made of Plexiglas, and textiles made from the skins of perch, salmon, and cod.<sup>24</sup>

Finally, along with all these activities, an intensive program for the collection and utilization of waste and scrap materials was carried on. Old tin cans, toothpaste and shaving-cream tubes, and other scrap metals were collected by house-to-house canvass. Waste paper was saved, collected, and reworked. Rags and other waste materials, such as bones, garbage, human hair, razor blades, horse chestnuts, and old coffee grounds were saved and put to use.<sup>25</sup>

*The Results of the Self-Sufficiency Program.* There is no doubt that the self-sufficiency program was successful in increasing the eco-

<sup>20</sup> *Ibid.*, p. 207

<sup>21</sup> *Ibid.*, p. 209

<sup>22</sup> P. T. Ellsworth, *International Economics*. New York: The Macmillan Company, 1938, p. 506.

<sup>23</sup> *Facts in Review*, February 13, 1940, p. 48.

<sup>24</sup> *Facts in Review*, February 19, 1940, p. 56.

<sup>25</sup> M. Y. Sweezy, *The Structure of the Nazi Economy*, p. 22.

nomic independence of the fascist countries Germany, for example, was said to be about 83 per cent self-sufficient with respect to foods by 1938.<sup>35</sup> Aluminum production increased from 97 to 166 thousand tons from 1936 to 1938, and, over the same period, non-ore production increased 70 per cent, lead and zinc ore production 24 per cent, oil production 25 per cent, wool production 19 per cent, hides and skins production 38 per cent, timber production 15 per cent, rayon production 40 per cent, and staple fiber production (for textiles) 220 per cent.<sup>36</sup> Both increased outputs of natural products and the production of large quantities of artificial substitutes decreased the dependence of the fascist countries on foreign sources of supply of vital materials.

However, this increased economic independence was purchased at great cost. The costs involved in expanding the output of natural products beyond the levels which would have been achieved in the absence of governmental interference were shown clearly in connection with the Battle of the Wheat in Italy. Crop rotations were upset, land well suited to raising other crops and poorly suited to raising wheat were transferred to wheat production, normal Italian exports of fruits, vegetables, and nuts were decreased and imports of butter, wool, meat, and eggs were increased, and it is doubtful that the increased production of wheat brought any net advantage to Italy with regard to self-sufficiency in foods or with regard to the balance of international trade. From 1926 to 1937, the number of hogs in Italy increased by 5 per cent, but the number of horses decreased 23 per cent, cattle 10 per cent, sheep 31 per cent, and goats 44 per cent.<sup>37</sup> The victory was very costly to Italian consumers. Domestic production of wheat could be increased to necessary levels only by increasing the tariff duty on imported wheat from 50 lire to 200 lire per quintal (or from about 68 cents to \$2.70 per bushel), and wheat prices in 1936 were 250 to 300 per cent above those of the world market.<sup>38</sup> According to some estimates, the Battle of the Wheat was won by reducing consumption just about as much as production was increased. And all this happened without much benefit to the average Italian farmer, since only the large landowners and prosperous farmers had much wheat to sell at the artificially high prices produced by the wheat campaign.

<sup>35</sup> *Facts in Review*, July 8, 1940, p. 308.

<sup>36</sup> *Facts in Review*, February 18, 1940, p. 41.

<sup>37</sup> W. Ebenstein, *Fascist Italy*, p. 201.

<sup>38</sup> *Ibid.*, p. 202.

Attempts to use relatively plentiful materials in the place of relatively scarce ones may have increased economic independence, but they tended to produce unsatisfactory results in other respects. If, for example, buildings of higher quality or lower cost could have been constructed by using more concrete and less steel, it is reasonable to suppose that builders would have realized this fact, and acted upon it, long before the adoption of the self-sufficiency program. The disadvantages of self-sufficiency were especially great in the case of the synthetic or artificial substitutes. In general, these synthetic products were more costly than the natural ones which they replaced. Textiles of cell wool which were as good as those made of natural wool could be turned out only at prohibitive cost, and even low-quality textiles of cell wool cost 30 or 40 per cent more than those made of natural materials. German synthetic gasoline cost between four and five times the world price, and synthetic rubber cost about four times as much as natural rubber. Butter produced from coal may or may not have been pure and better than natural butter, but even the Germans admitted that it was better not to say too much about its cost.

Again, the quality of the synthetic products was often much lower than that of the natural products. The fascist leaders, to be sure, spoke highly of the quality of some of their artificial substitutes. The butter made from coal was excellent, the synthetic rubber was of good quality, though rather hard, textiles made of fish skins ironed well and were guaranteed not to shrink, and the glass shoes were supposed to be as smooth and flexible as those made of first-class leather. On the other hand, some at least of the synthetic gasoline was supposed to be too poor for use in aviation, and clothes made from cell wool at a cost 30 to 40 per cent above that of clothes made from natural textiles were poor in quality. They were stiff, heavy, and disposed to retain moisture; they did not wash well, they kept their shape very poorly, and, judging by the fate of many German soldiers during their winters in Russia, they may have been far from perfect in the matter of affording protection against the cold. Probably the fascist leaders hoped that some day their synthetic products would be better and cheaper than the natural products, but this goal was apparently never realized in practice.

Even when an artificial material was of good general quality, it might differ from the corresponding natural product in some way which would bring difficulties in processing and manufacture. The

extreme hardness of synthetic rubber, for example, made it difficult to handle with the usual machinery and equipment, and both new kinds and greater quantities of machinery had to be used in processing it Again, large and numerous plants for producing the synthetic materials in the first place had to be set up, and the cost of constructing these facilities fell to a great extent on the old-established industries of the fascist countries As we noted in our discussion of credit and investment, large enterprises in various regular manufacturing industries were compelled to construct plants for producing synthetic materials or to subscribe heavily to the capital shares of plants set up for this purpose As a result, many enterprises and industries found it difficult to improve or even maintain their own productive facilities, and the quantity, quality, and cost of their own products were sometimes adversely affected

Finally, the production of synthetic materials, while bringing increased economic independence in some sectors of the fascist economies, caused new shortages in other fields Thus, the use of wood to make clothes, shoes, hardware, containers, and other products helped out in some respects, but it put great pressure on the German timber supply which, even before the self-sufficiency program, was described as insufficient to meet German needs fully The net gain obtained by transferring shortages from one field to another may not have been very great

The policy of economic self-sufficiency was especially unfortunate in the case of Italy, with her limited soil and natural resources, small total accumulation of capital, and artificially stimulated rate of population growth According to any logical standards, Italy would have been expected to gain from peace, free trade, and free migration Germany was in a somewhat better position than Italy to attempt a program of attaining national economic self-sufficiency, but the results of her program were just about what would have been expected on the basis of economic principles By refusing to accept the advantages of international specialization and exchange, both fascist countries secured an increased degree of economic independence at the cost of lowered real incomes and standards of living for their people

And the choice was a voluntary one The fascist leaders definitely preferred economic independence in preparation for war to higher real incomes and standards of living for the people, and the leaders got what they desired, as usual In the absence of the policy of plan-

ning and preparing for aggressive warfare, the difficulties with respect to international trade and foreign exchange which the fascist countries experienced in the post-1929 depression could have been overcome. And the irony of the self-sufficiency programs was found in the fact that, if the aggressive warfare for which the self-sufficiency programs were a preparation had turned out to be completely successful, Germany and Italy would have obtained direct access to most of the foods and raw materials that they lacked and the tremendous investments of land, labor, and capital necessary under the self-sufficiency programs would have become no longer useful.

#### QUESTIONS

- 1 "The situation of Britain with respect to international trade changed sharply from 1938 to 1916 and 1917" Explain
- 2 "Britain's postwar crisis in international trade and foreign exchange was due to her desire to live beyond her means and buy more than she could pay for" Show whether you agree
- 3 "Britain's postwar problems of international trade and foreign exchange resulted from her change from capitalism to partial socialism" Do you agree? Explain
- 4 How has Britain attempted to solve her problems of international trade and foreign exchange? Explain
- 5 "The foreign trade and balance of payments of both Italy and Germany were severely affected by the great depression which began in 1929" Explain
- 6 How did the fascist governments of Italy and Germany control international trade and related matters?
- 7 "Trading agreements between the governments of fascist Italy and Germany and those of other countries usually worked to the disadvantage of the other countries" Show whether you agree
- 8 How were export subsidies used by the governments of the fascist countries?
- 9 "The policies of fascist Italy and Germany succeeded in stabilizing foreign trade but at rather low levels" Do you agree? Explain
- 10 "The self sufficiency programs of fascist Italy and Germany included three parts or phases" Explain
- 11 "The experiences of the fascist countries indicate that the policy of national economic self sufficiency is a very costly one from the economic point of view" Show whether you agree
- 12 "The most costly phase of a policy of national economic self sufficiency is likely to be the attempt to increase the output of natural products, as in the case of Italy's Battle of the Wheat" Do you agree? Explain

- 13 "In view of the success of the fascist programs of national economic self-sufficiency, Britain might well adopt such a program as a way out of her current difficulties in connection with international trade and foreign exchange" Discuss
- 14 "In the absence of the program of planning and preparing for aggressive warfare, the difficulties with respect to international trade which Germany and Italy experienced in the post-1929 depression could probably have been overcome" Show whether you agree

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## CHAPTER 21

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### PUBLIC FINANCE

#### *Public Finance under Capitalism*

*Governmental Functions and Expenditures* In a capitalistic system, most phases of economic activity are supposed to be carried on by private individuals and firms on the basis of price relationships, rather than by organized society or government. However, even in such a system, governmental units perform a considerable number of functions which are more or less economic in character. The reason for this allocation of functions to government is suggested by the statement that "government, as a form of social organization, has developed because, in the long run, it has afforded the means of supplying men with certain services more efficiently and more economically than these could have been supplied by each for himself."<sup>1</sup> The delegation of the provision of such services to and their performance by the government may be regarded simply as a part of the division of labor.

The functions which are performed collectively through the government rather than by individuals are of several general kinds. Some services, such as the furnishing of protection against external foes or the maintenance of law and order within the country, would be very difficult, if not impossible, for the citizen to perform for himself. Others that could be and often are carried out by private firms are sometimes turned over to governmental units in the hope that they will thus be performed more efficiently or cheaply. Examples are found in the provision of water and electricity by municipalities. Thirdly, as Adam Smith said, the government has "the duty of erecting and maintaining certain public works, and certain public institutions, which it can never be for the interest of any individual."

<sup>1</sup> H. L. Lutz, *Public Finance* New York D. Appleton Century Company, Inc., 1936, p. 1

vidual, or small number of individuals, to erect and maintain, because the profit could never pay the expense to any individual, or small number of individuals, though it may frequently do much more than repay it to a great society."<sup>2</sup> For example, individuals as such would probably not be moved to set up institutions for dependents and defectives because their share in the resulting benefits would be too small or too long deferred.

While the government under capitalism does furnish us with some services or even commodities which we could obtain from private individuals and firms, our government is to be regarded largely as an instrument for overcoming to some extent the deficiencies of the capitalistic market and price mechanisms. Some complex wants, such as the desire for economic security, seem to baffle the ingenuity of the market and price mechanism altogether, but they nevertheless hold a relatively high position in the preference scales of many individuals. Since there is no way in which individual citizens can go out into the market and bid up the value of economic security so as to induce the economic system to furnish more of this desirable product, we are likely to rely on government for the expression and fulfillment of this want through a comprehensive program of social insurance or other devices. The government also helps to overcome the deficiencies of the market and price mechanisms by furnishing the individuals of the system with a means for expressing and fulfilling their negative preferences. If, for example, we do not wish to see people suffer from consuming impure and adulterated foods and drugs or noxious patent medicines, or want to keep people from being the victims of monopolistic business practices, fraudulent advertising, or the sale of worthless securities, there is comparatively little that we can do by means of the price mechanism. Certainly we cannot go into the market and, by paying a price of five or ten dollars, make sure that such undesirable practices will not be carried on and such undesirable commodities will not be produced and sold. But, if enough individuals have the same negative preferences, they can express them through governmental action.

It is not easy, in a capitalistic economy, to determine just how many functions should be delegated to the government, but certain general principles governing this matter can be stated. In the case of functions which can be performed either by government or by

<sup>2</sup> Adam Smith, *The Wealth of Nations*, Book IV, p. 286.

private individuals and firms, a function should be delegated to the government only when it appears that, having given adequate consideration to the necessary costs of administration in collecting and spending the funds through the government and to whatever is known concerning the efficiency of the government in question, the expenditure of a given sum collectively will result in a more adequate and economical service than could be obtained by a similar sum privately spent. However, this principle does not cover all cases, for some functions must be performed by the government or not at all. A more general principle would state that the government should perform such a number of functions and should collect and spend such an aggregate sum that the advantage in the form of satisfaction to be gained from any further functions and expenditures would not be sufficient to offset the disadvantage of loss of satisfactions (either direct, or indirect through the ill effects on business and productive activities) which would result from turning over the necessary additional funds to the government. Moreover, the aggregate expenditures of the government should be divided among the several governmental activities in such a way that no money will be spent for any one purpose which would result in a greater net satisfaction if it were added to the sum to be spent for some other purpose. These principles are not easy to apply in practice but the considerations set forth in them do seem to be those which should be borne in mind in making decisions concerning governmental functions and expenditures. And, of course, the expenditures of government should be necessary and appropriate to the functions which it undertakes to perform.

*Public Revenues* Governmental units sometimes borrow heavily over considerable periods of time and they may secure small amounts of money income from various enterprises which they operate, but taxation is the most important long-run source of the funds from which public expenditures are made. Several economic principles are available for the guidance of government in setting up a sound system of taxes in a capitalistic economy. The first and in many ways the most important test of a tax system is found in the question of whether it will furnish sufficient revenue. Even though a tax system were perfect in other respects, it could not be considered satisfactory if it did not provide the revenue necessary for the performance of essential governmental functions. A second principle is that of economy in collection. As was said many years

ago, every tax ought to be so contrived as both to take out and keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state.

Taxes should be simple so that they can be understood both by those who pay them and by those who administer the tax laws. Taxes should be certain both with respect to amount and with regard to time and manner of payment. Taxes should be collected at such times and in such a manner as will be most convenient for the taxpayer. A tax system should be elastic so that it can be made to yield larger or smaller amounts of revenue as governmental needs vary from time to time. In connection with all of these principles, the effects of taxation on the taxpayers and on business in general should be considered. While taxes may seem to meet all the tests directly, they should not be considered satisfactory in a capitalistic system if they are levied in such fashion or to such extent as to discourage business activity, curb individual initiative, or check unduly the accumulation of capital. However, there are usually great differences of opinion in a capitalistic system as to the exact point at which these undesirable effects are likely to show themselves as taxes are increased in number and severity.

A final principle of taxation suggests that the tax burden should be distributed among the taxpayers as equitably as possible. At one time, the principle that each person's contribution to the support of the government should be in proportion to the benefits which he received from the government found considerable favor. In more modern times, however, it is more commonly held that each individual should be taxed, for the most part, on the basis of his ability to make contributions to the support of the government and without much regard for the amount of benefit which he may receive from governmental activities. The most commonly accepted indicator of ability to pay was once the ownership of wealth but the emphasis has gradually been shifting to the receipt of income. In connection with the receipt of income as the criterion of ability to pay taxes, the most important question concerns the extent to which ability to pay increases as income increases. If one person has a taxable income of \$4000 while another has one of \$2000, should the first person pay exactly twice as much in taxes as the second, more than twice as much, or less than twice as much?

The answer to this question depends upon what happens to the marginal utility or importance of a given-sized unit of money in-

come to the individual as successive units of money income are received Economists commonly argue that the utility to be expected from the expenditure of a unit of money income diminishes as the total income of the individual increases The rational individual devotes the first units of money income which he receives to the satisfaction of his most important wants, while further successive units of money income must be devoted to the satisfaction of successively less important wants When the individual is forced to give up a certain part of his money income to the government in taxes, the satisfactions which he will surrender are those which are marginal or least important to him, and the magnitude of these marginal satisfactions will be smaller the greater is his total money income Thus it is claimed that an individual with an income of ten thousand dollars a year does not lose nearly so much satisfaction when compelled to give up one thousand dollars in taxes as does the individual with five thousand dollars when he contributes five hundred dollars to the support of the government, although it is clear that taxes are paid at the same rate in both cases This analysis of the diminishing and marginal utility of money income is not completely satisfactory, since it involves inter-personal comparisons of utility which cannot be made with great confidence and since it assumes that no significant differences exist in the capacities of individuals to experience satisfactions However, it is the basis for arguing that, whatever may be true of the burden imposed by individual taxes, the burden imposed by the tax system as a whole should be progressive with respect to income That is, taxes as a whole should take a greater proportion (and not merely a greater absolute sum) from large incomes than from small incomes

Just how progressive the burden of taxes should be with respect to income, in order to follow the principle of ability to pay, depends on some other considerations Some writers suggest that the principle of equal sacrifice should be followed This means that the burden of taxes should be so progressive that all individuals would experience an equal loss of satisfaction, or an equal amount of sacrifice, in paying taxes to the government In other cases, it is contended that the principle of least aggregate sacrifice would be more appropriate Following this principle would mean that each individual would be required to pay no tax whatsoever so long as the same amount of tax revenue could be obtained from another person with a smaller loss of satisfaction or sacrifice In this situation, any

given aggregate amount of revenue would be obtained with the smallest possible aggregate loss of satisfaction, or sacrifice, and rates of taxation would be steeply progressive.

**Public Debt** In general, the expenditures of government in performing its various functions should be covered by its revenues from taxation and the operation of public enterprises, so that governmental borrowing is unnecessary. However, in practice it may sometimes be impossible or undesirable to raise enough revenue from taxation and other sources to finance all the public expenditures which it seems essential to make, and public borrowing becomes necessary. There is nothing inherently wrong about public borrowing. When a great national emergency requires expenditures in excess of collectible revenues, a government would be unwise if it did not permit its budget to become unbalanced. If a man's house were on fire, he would not usually hesitate to call the fire department even if he had to pay directly the expenses of the department in putting out his fire and knew that this expenditure would unbalance his budget for the current month or year.

On the other hand, there may be great dangers, at least in a capitalistic system, in large continuing governmental deficits and increases in the public debt. If the public debt grows so large that it becomes most improbable that the government will be able to pay interest and repay principal as agreed, the citizens may lose faith in the government's financial soundness and the government may be unable to continue to borrow large sums from its citizens. If the government is then unable or unwilling to cut down its expenditures or increase its revenue from ordinary sources, it may have to print paper money with which to pay its bills. Such inflationary tactics on the part of the government may lead the economy to a breakdown from which it may not recover for many years. On the other hand, the extent to which it is possible for a large public debt to become a crushing burden on future generations of citizens is frequently exaggerated by the opponents of deficit financing.

**Public Expenditures in the United States** The public expenditures of all types of governmental units in the United States have increased enormously in recent decades. Even in the peacetime years from 1934 through 1940, the expenditures of the federal government ranged from 6 to almost 9 billion dollars per year—figures which may be compared with total federal expenditures of \$517,000,000 in 1903 and \$725,000,000 in 1913. However, the large ex-

penditures of the depression years were small indeed by comparison with those which were yet to come During World War II, federal expenditures skyrocketed to a peak of \$100,405,000,000 in 1945, before declining to \$63,714,000,000 in 1946, \$12,505,000,000 in 1947, and \$39,326,000,000 in 1948.<sup>8</sup> In these years, expenditures for national defense (including interest on the public debt and veterans' pensions and benefits) made up an extremely large part of total federal expenditures The expenditures of state and local governments in the United States have also increased rapidly over the years, although the increases have not been so spectacular as those in federal expenditures

A part of the great increase in public expenditures in the United States may be attributed to increases in the population of the country The performance of even the same number of functions as formerly for an increasing population is likely to result in a proportional, if not a more than proportional, increase in public expenditures, and the growth of population is likely to bring about an expansion in the number of needs which it appears necessary or desirable to satisfy collectively rather than individually Again, public expenditures are expressed in terms of money, and changes in the general price level and the purchasing power of money constitute another cause of the growth of public expenditures Even though there is no increase in the number of governmental functions or in the intensity with which they are carried on, governmental expenditures must increase ordinarily with increases in the prices of goods and productive factors which the government must secure in order to carry on its functions

However, after due allowance has been made for growth of population, changes in the price level, and possibly other factors, the chief explanation of increasing public expenditures is to be found in the continually growing number of functions being performed by federal, state, and local governments and the increased intensity or thoroughness with which the functions are carried on The expansion in functions in turn has been largely the result of such things as the great and pressing economic problems that have arisen as our economic system has increased in size and complexity, the growing conviction that social welfare can and should be advanced by collective action through government, and the more recent notion that the government can and should assume direct responsi-

<sup>8</sup> *Federal Reserve Bulletin*, August, 1948, p. 991

bility for the satisfactory operation of the economic system as a whole

In the case of the federal government, important increases in functions and expenditures occurred during the years of the great depression after 1929. For one thing, it became a federal function to care for the unemployed, and federal activities in their behalf, through the Public Works Administration, the Civil Works Administration, the Civilian Conservation Corps, the Work Projects Administration, and assistance given to the states in providing direct relief, cost something like 26 billion dollars from 1933 to 1941. Through a great variety of agencies, the federal government attempted to regulate agricultural production, raise the prices of farm products, refinance farm mortgages, and lend the farmers credit on their holdings of various crops. Expenditures for these purposes amounted to more than a billion dollars in some years and totaled over 5 billion dollars from 1933 to 1941.

Other federal activities designed to promote recovery were less costly than those already mentioned. They included financial assistance to railroads, banks, and other institutions through the Reconstruction Finance Corporation, the refinancing of the obligations of home owners other than farmers, the attempt to promote the rehabilitation of industry and business through self-regulation under the National Recovery Administration, insurance for bank depositors through the Federal Deposit Insurance Corporation, the Subsistence Homestead Projects, and the Emergency Housing Program. At the same time the federal government undertook other activities which seemed to be dedicated to reform rather than, or in addition to, recovery from the depression. Examples included the regulation of the issuance of new securities and of the activities of the security exchanges through the Securities and Exchange Commission under laws of 1933 and 1934, the regulation of the public utility industry through the Securities and Exchange Commission and the Federal Power Commission under the Public Utilities Act of 1935, and various activities for the benefit of labor under the National Labor Relations Act of 1935 and other laws.

Most of the depression activities of the federal government were still going full blast when World War II began. When the United States entered the war, governmental control over the economic activities of the country increased greatly and soon dwarfed anything that this country had ever before experienced. Long before

the war was over, agencies of the federal government were controlling output in many branches of production, the prices of commodities and services, wages and salaries, rents, the allocation of essential materials and equipment among industries and businesses, the allocation of labor among industries, businesses, and the armed forces, industrial relations in many industries, imports and exports, the apportionment of certain scarce consumers' goods among the individual citizens, and many other things. While many persons questioned whether all these governmental controls were essential to the prosecution of the war and whether certain controls were well suited to the objectives which were being pursued, the wartime functions and expenditures of the federal government were in general accepted with good grace by the people as being more or less inevitable in such an emergency period.

During the war period, many people in this country apparently came to the conclusion that, while some controls over economic activity imposed by the federal government in wartime should be relaxed in the postwar period, the federal government must continue to assume responsibility for the successful operation of the economy as a whole. Governmental functions proposed in this connection included such things as the guaranty or underwriting of full employment by the government and the provision of a system of social security, popularly known as the "cradle-to-grave" variety, to cover many more people, provide against more risks, and furnish much larger benefits than the existing system.

It is not always easy to decide whether the functions and expenditures of our various governmental units are justified on the basis of the proposed criterion for public functions and expenditures. It is not to be supposed that under modern conditions we can safely neglect such matters as education, roads and highways, and the provision of institutions for delinquents, dependents, and defectives, and, on the whole, the expenditures for these and other social welfare purposes may be expected to bear up well under the proposed test for public expenditures. In other words, the activities which cause these expenditures may be expected to create enough satisfactions for the receivers of the services, or for society as a whole, to more than make up for losses of satisfactions to individuals or damage to business which may result from the collection of the funds necessary to sustain these activities. Much the same thing is probably true of most of the regulative activities of the federal gov-

ernment and other governmental units Most of these activities are expressions of various negative preferences of the masses of citizens, and, if they do not actually create satisfactions, are likely in most cases to prevent losses which would exceed those of the taxpayers who must furnish the funds necessary to carry on these regulative activities

There is more doubt concerning the largest and most expensive activity of the federal government—the provision of protection or national defense Under ordinary circumstances and from the strictly economic point of view, war is an extremely costly and most unsatisfactory method of settling disputes among nations Modern warfare almost inevitably brings great economic losses, and not increasing totals of satisfactions, to all participating nations From the national point of view, it may be possible to justify the tremendous economic losses which result from war as being necessary in order to prevent other and still greater losses, such as those which we would sustain if aggressor nations were able to take our land and resources from us and destroy our institutions However, from the point of view of the world as a whole, the billions of dollars which have been and are being spent for wars and armaments have been and are economic waste

What shall we say of the depression activities and expenditures of the federal government? From the point of view of a direct comparison of satisfactions, many of them would probably pass muster Consider, for example, relief or work relief for the unemployed, which was the largest and probably the most severely criticized of the depression expenditures of the federal government So far as governmental assistance was received by those who really needed it, it is hard to believe that these expenditures did not give more satisfaction to the recipients of the government's aid than they took away, or will take away, from the taxpayers However great the pangs suffered by those who have paid or must pay taxes to cover relief expenditures, they are doubtless less painful than the pangs of death by starvation or exposure

However, when we consider the indirect effects of the depression activities and expenditures, the answer is not so clear The heavy expenditures had to be financed by either taxation or borrowing To the extent that taxation was used, high taxes tended to cut into employment-creating private spending for consumption and investment as well as unnecessary saving Moreover, some individuals in

the higher tax brackets may have been rendered unwilling to put capital funds into risky ventures, since any gains which they might make would have to be shared with the government, while any losses they might suffer would be almost entirely their own. To the extent that borrowing (deficit spending) was used to finance the governmental expenditures, business confidence may have been affected and fears of later higher taxes aroused, with adverse effects on the amount of production and employment furnished by private industries and businesses.

Funds for relief or work relief may have been used in some cases for political purposes rather than to promote recovery from the depression, and the receipt of governmental assistance probably weakened the morale of some persons and made them anxious to make a "career" of the WPA or to "retire" on relief, rather than to shift for themselves in private employment. The laws of 1933 and 1934 may have cleansed and purified the issuance of securities and the operation of the security exchanges, but according to some authorities, they also brought the issuance of new corporate securities almost to a standstill and greatly weakened the functioning of the security exchanges. Though the activities in behalf of labor greatly improved the bargaining position of employed workers, they may have made entrepreneurs less willing than they would otherwise have been to undertake production and furnish employment. Direct competition with private business by governmental enterprises or agencies, or even the threat of such competition, and the general attitude of hostility toward private industry and business on the part of the federal government, may have had similarly detrimental effects.

Other examples could be given, but those presented above may be adequate to suggest that the assumption by the government that the capitalistic system could not handle the situation may have led to governmental activities which increased the probability that the capitalistic system would be unable to operate successfully. It is impossible to know whether our economic system as a whole was actually better off by, say, 1940 than it would have been if the federal government had not assumed responsibility for its operation and for the promotion of recovery in 1933. However, it is clear that the degree of recovery from depression which was effected under governmental control was disappointing, and that the recovery was far from complete at the outbreak of World War II.

In evaluating governmental activities and expenditures which are proposed for the postwar period, such as the guaranty of employment and the provision of almost complete social security, it is not enough merely to compare the gain in satisfactions by the beneficiaries of these policies with the loss of satisfaction suffered by the taxpayers. As in the consideration of depression activities and expenditures, we must consider the effects on private businesses and industries and on the economy as a whole. The danger that these expansions in governmental activities and expenditures might lead us in the direction of a planned and controlled economy is far from negligible, for large expenditures for the proposed activities would have to be added to the already heavy expenditures for the armed forces, veterans' pensions and benefits, interest on the public debt, and the regular operation of governmental departments.

Just how large the annual expenditures of the federal government would have to be with these new projects included is uncertain, but most estimates call for federal expenditures far larger than those to which we have been accustomed in peacetime. Whatever the exact amount might be, the large expenditures would have to be financed by means of taxation if we did not wish to add to the already overgrown federal debt. This would call for the continuation of very high levels of taxation, which might be as high as, or higher than, those that prevailed during the latter years of World War II.

The point to be made in this connection is that our economic system perhaps could not continue to operate in capitalistic fashion in peacetime if the government should find it necessary to take a large part of the incomes of individuals and the earnings or "profits" of business enterprises of all types, especially if business enterprises were left to bear unassisted the greater part of any losses which they might encounter. Moreover, such a situation would be most unfavorable for the expansion of the economy and the foundation of new enterprises based on private capital. And this discussion of public finance ignores the important direct question, discussed in Chapter I7, of whether the government could maintain full employment and a complete system of social security in any case without assuming virtually full control over the operation of the economic system as a whole.

*Taxation in the United States.* The tax revenues of the federal government and other governmental units in the United States have also increased rapidly in recent years, though not so rapidly as

public expenditures on the whole. In 1918, the total revenues of the federal government amounted to \$16,362,000,000. Of this total, personal income taxes contributed over 45 per cent, corporation income taxes and profits taxes about 22 per cent, excise taxes almost 16 per cent, social security taxes 5 per cent, and estate and gift taxes about 2 per cent.<sup>4</sup> Federal revenues in 1918 provided a welcome surplus above total federal expenditures of \$19,326,000,000.

The various state governments of the United States received total tax revenues of \$1,253,300,000 in 1915. Of this total, sales and use taxes produced 36.9 per cent, incomes taxes 19 per cent, gasoline and motor fuel taxes 16.5 per cent, motor vehicle licenses 9.5 per cent, business licenses 6.2 per cent, property taxes 5.4 per cent, and inheritance, estate, and gift taxes 3.1 per cent. Local governmental units in the United States still depend very largely on the general property tax, which produced 87.5 per cent of their total tax revenues in 1944.<sup>5</sup> Then other tax revenues were derived from scattered sources, such as other property taxes, business and non-business licenses, and poll taxes.

It is not possible for us to comment in detail on each of the various types of taxes which are used in the United States, but we may say that, on the whole, taxation in the United States at present seems to conform rather well to the principle of ability to pay. Since about 70 per cent of the total federal revenues are received from taxes which are at least nominally progressive, and since federal revenues are several times as large as those of state and local governments combined, it is possible to conclude that taxation in the United States at present is on the whole progressive in operation. In other words, the greater part of our total tax revenue is received from taxes which take a larger part of large than of small incomes.

*The Public Debt of the United States* The taxation system of the federal government has been defective in most recent years from the point of view of fiscal adequacy, and the same thing has been true to a lesser extent of the taxation systems of state and local governments in the United States. The federal budget was unbalanced from 1931 through 1946, and the annual deficits ranged from 462

<sup>4</sup> *Ibid.*, p. 991.

<sup>5</sup> *The Economic Almanac for 1946/47*, p. 302.

<sup>a</sup> *Ibid.*, p. 315.

million dollars in 1931 to almost 56 billion dollars in 1943.<sup>7</sup> As a result, the federal debt was increased rapidly from \$16,801,000,000 in 1931 to \$48,961,000,000 in 1941 at the beginning of the war and \$269,422,000,000 in 1946.<sup>8</sup> It rested at \$251,168,000,000 in July, 1948.<sup>9</sup>

In our capitalistic economy there can be no sound objection to governmental borrowing to meet an emergency, when revenues fall short. As we have said before, if a national emergency requires expenditures in excess of collectible revenues, the federal government would be foolish not to permit its budget to become unbalanced. When a man needs a surgical operation, he does not hesitate to call in the surgeon merely because the cost would unbalance his budget for that year. On the other hand, while the use of sulfa drugs may be indicated for pneumonia, they would scarcely prove beneficial as a steady diet. Continuing deficits of many billions of dollars per year may lead to most severe inflationary pressure if, indeed, they do not result in the destruction of the government's credit.

During World War II, our federal government, anxious to make total expenditures far in excess of the sums which it was thought possible or feasible to collect in taxes or obtain through direct sales of bonds to the people, resorted to sales of bonds to the banks in order to obtain the necessary funds. The banks paid for these bonds by creating demand deposits for the government to spend. In this way, the government obtained large sums of purchasing power without reducing the funds available for civilian spending, and the total of government and civilian purchasing power became much larger than necessary to take off the market at stable prices all the commodities and services the economy could produce. The situation which was created was about as inflationary as though paper money had been printed to finance governmental expenditures, except that people apparently are not driven into as great a panic by the creation of demand deposits as by the printing of paper money. A tremendous inflation of prices was avoided during the war period by resorting to direct price control and other devices, but these measures merely postponed the problem to the postwar period and did not eliminate it.

<sup>7</sup> Board of Governors of the Federal Reserve System, *Borrowing and Monetary Statistics*, pp. 509, 510, 513. *Federal Reserve Bulletin*, September, 1947, pp. 1401-1403.

<sup>8</sup> *Federal Reserve Bulletin*, August 1948, p. 99.

Another objection to our rapidly growing public debt runs to the effect that we shall be passing on to our children and grandchildren a staggering burden of debt which they will have to pay, to their own great detriment. This contention is difficult to evaluate. Clearly, in the sense of *real income*, future generations may not suffer from a large public debt incurred now. If the government borrows to buy wheat to feed its starving people, the wheat is taken not from the crops of thirty or fifty years hence, but from present supplies. If the government uses borrowed funds to induce farmers to plow cotton under current crops (and not those which our children will harvest) are reduced. When the government spends billions of borrowed dollars for war goods, it causes a shortage of consumers' goods here and now, rather than in the more or less indefinite future.

From the financial point of view, it is certainly true that the government will have to collect taxes in the future in order to pay interest on its obligations and possibly to pay part of the principal, but at the same time these amounts will be paid to the owners of the government bonds which represent our public debt. If the people who own the bonds also pay the taxes, even private individuals may "break even" on the process. But whether *individuals* gain, lose, or break even, it is clear that the *nation as a whole*, in paying off the public debt, merely transfers money from one pocket to another so long as the entire debt is held within the country. Such transfers, it is often argued, should not be very harmful.

On the basis of these and other arguments, some writers are inclined to scoff at the idea that our large public debt will give us trouble in the future. The size of the debt is a matter of small importance, since "we owe it to ourselves." While individual bondholders will need to be paid off from time to time, the principal sum of the debt as a whole will never have to be paid, and our only concern should be the size of the interest payments in relation to our national income. Indeed, some writers consider it desirable to have a continually growing public debt, on the ground that large governmental expenditures in excess of current revenues will insure the existence annually of a total sum of purchasing power large enough to take off the market all the commodities and services which the economy can produce at full employment. If we can keep the national income constantly growing, even a total of interest pay-

ments which steadily increases in absolute size will not be a very severe burden

However, such a light-hearted attitude toward the future burden of the public debt may be far from completely justified When taxes are collected to pay interest on the debt or to repay principal, they may be so large in amount or be collected in such ways as to hamper and restrain production and employment and impair the effectiveness of our productive facilities Indeed, these taxes may contribute significantly to a total burden of taxation which is so heavy that our economic system cannot support it and still operate in capitalistic fashion. The collection of taxes and payment of interest may also result in a large and possibly undesirable transfer of income from some income groups to others

Increases in the total of fixed income payments in the economy, such as interest payments on government bonds, tend to concentrate the risks of the system on those relatively few incomes which are drawn from the operation of business enterprises and the investment of venture capital It has been estimated that the annual interest on a federal debt of 300 billion dollars would exceed the total of interest on private debts plus rents in a full-employment national income, and would equal one-fourth of the total business income (dividends, plus income of unincorporated businesses plus agricultural income)<sup>9</sup> With our banks and other financial institutions loaded with government bonds, a general rise in interest rates which would cause government bonds (with their low fixed rates of interest) to depreciate sharply in value would be a matter of serious concern Finally the political implications of having a large class of persons dependent upon interest on government bonds for a considerable part of their income may be anything but favorable The size of the public debt *may* be a matter of considerable importance in the future even if we do "owe it to ourselves"

### *Public Finance under Socialism and Communism*

**Public Expenditures** The theory of modern socialism does not have a great deal to offer on the subject of public finance, but it is not difficult to make out, at least in a general way, what a socialistic system of public finance would be like A socialistic economy is not

<sup>9</sup> *Financing American Prosperity* New York, Twentieth Century Fund, 1915, pp. 138-139

one in which private individuals and firms perform most economic functions and produce most commodities and services, while only a few economic functions are delegated to government. Rather, in a socialistic economy, the citizens receive almost all their incomes collectively and the government, operating in the name of the people as a whole, is the only enterpriser of any great significance. Even in ordinary times, the expenditures of a socialistic government would bulk very large in relation to national income, since it would have to make expenditures for operating the various industries and businesses of the country as well as for the carrying on of functions which are ordinarily regarded as more strictly governmental. Just how governmental expenditures would be divided between ordinary governmental functions (such as national defense, the operation of ordinary governmental departments, and various social services and cultural projects) and the function of operating the economic system of the country cannot be determined on an *a priori* basis.

*Public Revenues* Since the government of a socialistic economy would make about all the expenditures necessary for the operation of the economic system, it would receive as revenue the proceeds from the sale of the commodities and services turned out. Whether it would need to levy any taxes would depend on the manner in which the leaders decided to operate the economic system. If the government simply directed the productive agents of the system into national defense activities, various social and cultural services, the operation of governmental departments, and the production of planned quantities of commodities and services, and on the other hand took care to pay out to the citizens only such amounts of money income as were necessary to purchase available quantities of consumable economic goods on the market, it would not be necessary to levy any taxes.

On the other hand, if the government paid out money incomes to the citizens which represented the aggregate value of all production, including not only the value of commodities and services which were to be sold to the people but also the value of new productive facilities which were to remain in governmental hands and the value of all commodities and services which were to be furnished or rendered to the people without direct charges or prices, it would then be necessary to levy taxes on the people to absorb those portions of money income which were not required to buy available commodities and services on the market. In practice, the latter course of

action would probably be followed, since it would be desirable to have all the economic activities of the system pass through the accounting and money mechanisms Furthermore, it would be desirable to have the citizens know that the commodities and services which they apparently receive from the government without charge are really costly in the sense that they require the use of scarce agents of production, and to keep the people interested in all activities of the government and conscious of their part in governmental activities These results would probably be achieved if the government paid out large amounts of money income to the people and then recovered a part of this income through taxation

Of course, a part of the excess money incomes of the people could be absorbed by selling commodities and services to them at prices well in excess of costs, by selling them government bonds, or by inducing them to put surplus funds in governmental savings banks However, it is probable that taxation would be used to a great extent for this purpose A socialistic government would probably use taxes of familiar types for there seems to be no reason for thinking that such a government would be able to invent new kinds of taxes which had never occurred to the hard-pressed leaders of capitalistic governments Moreover, the familiar principles of taxation would seem to be valid for a socialistic system, though the principle of equity in the distribution of the tax burden among the individual citizens would not require the use of highly progressive taxes for raising a large part of the tax revenue of the government Almost any kind of taxes could be equitably used in a socialistic system Since differences in incomes between individual citizens would be relatively small, even a general sales tax would bring about approximately equal burdens of taxation from one citizen to another We should not be surprised, then, if a socialistic economy employed taxes whose use would be condemned in a capitalistic system with its highly unequal individual incomes

**Public Debt.** In a capitalistic system, the expenditures required to perform the governmental services which seem essential in a particular year or series of years may well exceed the total revenues which it is possible or wise for the government to try to extract from the private incomes of the citizens In a socialistic economy, however, the government both performs ordinary governmental functions and operates the economic system as a whole Being in complete command of the situation and handling almost the entire money income

and outgo of the country, it should always be possible for a socialistic government to balance its budget, if it desired to do so. Balancing the budget would seem to be more nearly a problem of arithmetic than one of public finance in the ordinary sense. On the other hand, an unbalanced budget would mean comparatively little in a socialistic economy. Suppose, for example, that the taxation system failed to absorb a sufficient part of the money incomes of the people and left them with more than enough money to purchase all available commodities and services on the market. This would only mean that the individual citizens would have more money than they could use in purchasing. They could not even have the fun of bidding up the prices of commodities and services with their excess money incomes. This situation might cause some dissatisfaction but it could hardly be very serious. Moreover, a shortage of revenues from taxation could scarcely cause the government to curtail any of the essential functions which it had planned to perform.

In similar fashion, a surplus of revenue from taxation would not have much significance. In fact, in the large sense, a surplus of governmental revenues could scarcely exist. The revenues of the government from all sources could not in general exceed the total amount of money income paid out to all the citizens, nor could all available commodities and services be sold to the citizens for a greater total sum of money than that which was left in their hands after paying all taxes to the government. However, the amounts taken from the citizens in taxes could be so great as to leave them with money incomes which were insufficient for the purpose of buying all commodities and services available on the market at the prices set upon them by the government. This situation might also cause dissatisfaction but it could be quickly remedied by adjusting the prices of consumable commodities and services on the market. And, of course, the fact that tax revenues were larger than usual would not be expected to stimulate a socialistic government to undertake any functions other than those which had been planned.

In view of the power of a socialistic government to balance its revenues and expenditures, it is difficult to see how it could be forced into an extensive program of public borrowing. On the other hand, there is nothing to prevent such a government from borrowing from its citizens if it desired to do so, and governmental borrowing, if it occurred, would probably proceed on the basis of familiar methods and practices. It would be surprising if the public debt of

a socialistic government ever became as great, relative to national wealth and income, as those of most capitalistic governments, and it would certainly not grow to the point where it would endanger the confidence of the people in the solvency of their government

### *Public Finance in Soviet Russia*

**The Budget.** In Soviet Russia, public finance plays the important part which would be expected of it in a socialized economy, and the national budget provides for the accumulation and distribution of the national income. The national budget is in reality a consolidated budget which provides for the expenditures and revenues of federal, republic, and local units of government. Financial relationships between these governmental units are rather indefinite and individual items of expenditure and revenue have been known to pass back and forth between these units from one year to another. The annual national budget, both with regard to revenues and expenditures, is closely connected at every point with the annual economic plan, and both are ordinarily approved together. As time has gone on, the national budget has accounted for a greater and greater proportion of the total financial operations of the country.

**Public Expenditures** Both governmental expenditures and revenues have had an extremely rapid growth in Soviet Russia under the planned economy. If the expenditures and revenues of 1928 are taken as 100, those for 1933 amounted to 545.6, those of 1938 to 1574, those of 1941 to 2676, and those of 1948 to 5058. Though expenditures and revenues are stated in terms of current rubles of fluctuating purchasing power, it is clear that changes in the value of the monetary unit cannot have accounted for any large part of these tremendous increases in expenditures and revenues. Two factors have been responsible for most of the increase. First, the economic activities of the country have been brought more and more under governmental control so that account must be taken of them in the national budget. This is suggested by the fact that the rate of increase shown by the budget has been greater than that of national income or retail sales. In the second place, the productivity of Russian industries and the general scope of economic activity have increased greatly over the years and, since the operation of the economy is largely in the hands of the government, this increase has been

rather automatically reflected in the revenues and expenditures of the government.

Total governmental expenditures amounted to 307 billion rubles in 1945.<sup>10</sup> As might be expected for this war year, expenditures for national defense occupied first place in the budget and required 45 per cent of total expenditures. Expenditures for social and cultural services, including education and training, public health, physical culture, social insurance benefits, and other items, took second place in 1945 and accounted for 21 per cent of total expenditures. While there were several minor sources of funds for social and cultural expenditures, the greater part of these expenditures was financed by appropriations from the national budget.

Third place in the list of expenditures in 1945 was held by those for the financing of the national economy, which made up 19 per cent of total expenditures. Industries, agriculture, forestry, transportation, posts and telegraph, municipal services, housing, trade, and other branches of economic activity were financed very largely by appropriations from the national budget. The grants made to these various fields of activity were for a considerable number of purposes, but 90 per cent of all allocations were for (1) capital investment, or the construction of productive capacity, and (2) the endowment of new enterprises with working capital and allocation of supplementary funds to enterprises already in operation.<sup>11</sup> Expenditures on governmental administration, the court system, and other ordinary departments of government, plus interest on the public debt, required 15 per cent of total budget funds in 1945. Total governmental expenditures in 1948 were scheduled to amount to 388 billion rubles, of which sum 66 billion rubles, or 17 per cent, were to go for national defense.<sup>12</sup>

*Public Revenues* Most of the income of the Soviet Russian government—74 per cent in 1945—is derived from the operation of the national economy rather than from direct taxes on the incomes of the individual citizens, though some of the principal methods of deriving income from the operation of the national economy are also dignified by the title of taxes. Total governmental revenues amounted to about 307 billion rubles in 1945, and the largest single revenue producer was the turnover tax, which yielded 38 per cent

<sup>10</sup> Statistics on expenditures in 1945 are from *The Soviet Union Today*, p. 47.

<sup>11</sup> A. Baykov, *The Development of the Soviet Economic System*, p. 385.

<sup>12</sup> *The Champaign Urbana News Gazette*, February 1, 1948.

of total revenues<sup>13</sup> Since 1945 was a war year and internal trade operated on a highly restricted basis, the turnover tax produced a much smaller proportion of total revenues than in earlier years In 1941, for example, it brought in 60 per cent of total revenues

The turnover tax is applied in simple fashion That is, the final prices which the government sets on all kinds of goods include the basic costs of production, transportation, and distribution, the planned profits, if any, of the producing and distributing enterprises, special taxes in some cases, and last, but not least, the turnover tax The tax represents the difference between the total cost of production of a commodity and the price which it brings as an article of general expenditure on the market The tax is paid to the government but once on each good, either at the firm production or the wholesaling level, though the burden falls eventually, of course, on the final consumer

The turnover tax is levied on practically all commodities of any importance, but at widely varying rates In 1945 it made up only 5 per cent of the selling price of some commodities, such as iron and coal, but amounted to 83 per cent of the selling price of vodka Many of the tax rates are, of course, extremely high A turnover tax which is 20 per cent of the selling price increases the cost of the good to the consumer by one-fourth, and one of 83 per cent makes the cost to the consumer about six times as great as it would have been otherwise As the tax has been applied in the past, the consumers, in buying a kilogram of bread for 85 kopecks, have paid as little as 21½ kopecks for costs of production and distribution plus profits and as much as 63¾ kopecks of turnover tax Similarly, a price of 42 rubles for a kilogram of sugar has at times yielded 63 kopecks for the producers and 3.57 rubles for the turnover tax<sup>14</sup>

The turnover tax has had rather obvious advantages from the point of view of the Russian government It is simple, it is collected quite automatically and with little cost, and it has produced tremendous amounts of revenue In the early days of the planned economy, when most Russian industries were struggling and inefficient, a great advantage was found in the fact that the turnover tax yielded its revenue regardless of whether individual firms and industries were efficient or inefficient, had high or low costs of production, and made or did not make profits Moreover, it is sometimes argued that

<sup>13</sup> Statistics on revenues in 1945 are from *The Soviet Union Today*, pp. 46-47

<sup>14</sup> A. Yugov, *Russia's Economic Front for War and Peace*, pp. 130-131

the tax distributes its burden quite justly and equitably among the individual citizens. This would actually be true if all Russian citizens received about the same amounts of money income, if they spent virtually all these incomes for articles subject to the tax, and if the tax were applied at about the same rate to different commodities and different grades of the same commodity.

In actual practice, it may be contended that money incomes differ enough from one individual to another in Russia to make the turnover tax quite regressive in operation. If this is true, the burden of the tax is not distributed according to the principle of ability to pay, but falls relatively more heavily on persons of small income than on persons of large income. This argument is fortified by other considerations. The tax falls at heaviest rates on foods and other articles of mass consumption, and it is applied at heavier rates to the cheaper grades of commodities than to the more expensive grades. Moreover, as Russian industries have been able to increase their efficiency and lower costs of production, the government has been content to allow its tax revenues to increase instead of lowering prices for the benefit of its needy consumers.

Another part of the revenues derived from the national economy is produced by the profits tax. The part of the final selling prices of commodities which is received by the producing enterprises is often intended to cover not only basic planned costs of production but also planned profits. Each enterprise has a right to retain a part of its profits for such purposes as capital investment, increase of working capital, and the maintenance of the director's fund, but the government also takes a large part of the profits. Profits taxes are payable on the actual rather than the planned profits of enterprises, but the rates of the tax, varying from 10 to 81 per cent for different classes of enterprises, are fixed on the basis of the financial plans of the enterprises in each year.<sup>10</sup> Profits taxes produced 7 per cent of total revenues, much less than the usual proportion, in 1945.

The rest of the revenues obtained from the operation of the national economy come from social insurance taxes (paid entirely by the enterprises), customs levies, and compulsory deliveries in kind and other exactions paid by the farmers. Goods imported by the state trading monopoly often have taxes applied to them before they are made available to the domestic economy and these so-called customs levies produced 9 per cent of total revenues in 1945. The

<sup>10</sup> A. Brykov, *The Development of the Soviet Economic System*, pp. 374-375.

social insurance taxes yielded 3 per cent of total revenues, and the tributes exacted from agriculture yielded 17 per cent of total revenues.

Direct taxes on the population are relatively unimportant in the Soviet Russian revenue system, yielding some 15 per cent of total revenues in 1945. Part of this revenue came from income taxes, which were progressive with respect to the amounts of income received by individuals and graduated also with respect to the sources of the incomes. In other words, a given amount of income derived from private activities was taxed more heavily than the same amount obtained from employment in state or cooperative enterprises. Another part of governmental revenues obtained directly from the population came from the so-called cultural and housing welfare tax. Governmental revenues were scheduled to reach 428 billion rubles in 1948.

**Public Debt** Revenues from taxation were not enough to cover total governmental expenditures in 1945, and the Russian government chose to make up the difference by public borrowing instead of by increasing taxes. Funds obtained by borrowing amounted to 11 per cent of total revenues. Prior to 1940, the Russian government did not depend heavily on borrowing from its citizens, and the public debt was very small. Before the end of 1941, however, it amounted to 47 billion rubles, and by 1946 it was estimated at 167 billion rubles.<sup>16</sup> Soviet Russia has virtually no external debt, having repudiated the debts of the previous regime.

According to the Russian authorities, each issue of government bonds is eagerly snapped up by the people, although interest rates are low on the interest-bearing bonds, while other issues pay no interest but rather entitle the owners to participate in an annual lottery in which the total prizes awarded amounted to 4 per cent of the face value of the bonds. The 12 billion ruble war loan of 1943 raised 20 billion rubles and the 25 billion ruble loan of 1944 realized 29 billions. The eagerness of the Russian people to buy government bonds is in reality rather artificial. In fact, subscriptions to bonds may almost be regarded as taxes on which the government sees fit to pay interest or award prizes.

When an issue of bonds comes out, a certain share is allotted to governmental enterprises, which must pay for the bonds out of their

<sup>16</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 135, and *Communism In Action*, p. 88.

profits Savings banks are required to invest their deposits in the bonds. The bonds are also sold to the individual citizens on a supposedly voluntary basis, but actually the citizens are virtually compelled to buy them. In some cases, deductions of certain percentages of the workers' pay are made for this purpose, and in other cases they pass resolutions, at the suggestion of representatives of the Communist Party, agreeing to buy the bonds. However, the bonds owned by individuals can be mortgaged at the savings banks for periods up to six months, and they can be bought and sold freely, except for speculative purposes. They can be donated and bequeathed, and any income derived from them is free of taxation.

### *Public Finance in Britain under Partial Socialism*

**Public Expenditures** Changes in the public finances of Britain, since the arrival of partial socialism under the Labor Government in 1945, have been less revolutionary than might have been expected. Total expenditures of the cental government for 1948 were scheduled to be £2,976,000,000.<sup>17</sup> This total represented a reduction of about 51 per cent as compared with 1944, but was still between three and four times the total of £833,000,000 spent in 1937. Interest on the public debt was to absorb almost 17 per cent of total expenditures, national defense over 23 per cent, and civil government departments and activities over 57 per cent. The same functions required about 7, 83, and 8 per cent, respectively, of total expenditures in 1944, the last year before the Labor Party came into power. Expenditures for 1948 were to include £400,000,000 for food subsidies, and these, together with amounts spent on social services, meant that the government would be making a contribution of 24 to 28 shillings a week on the average to each household.

**Public Revenues** Total revenues of the cental government were estimated at £3,765,000,000 in 1948, an increase of more than 16 per cent over 1944 and more than four times the 1937 total. The budget surplus for 1948 was scheduled to be £789,000,000. Income taxes were to furnish about 37 per cent of total revenues, death duties a little over 4 per cent, profits and excess profits taxes about 7 per cent, and customs duties and excise taxes over 14 per cent. In

<sup>17</sup> All data on British public finance, unless otherwise noted, are from *Britain's Budget* (New York: British Information Services, 1948), pp. 1-6.

1944 these types of taxes produced 43, 3, 16, and 33 per cent, respectively, of total revenues

The socialist philosophy of the Labor Government may be indicated by some of the changes which were made in the tax structure for 1948. In connection with the income tax, the total exemption limit was raised from £120 to £135 and the earned-income credit was increased from one-sixth of earned income (up to £250) to one-fifth (up to £400). In 1947, the first £50 of taxable income was taxed at 15 per cent, the next £75 at 30 per cent, and the rest at the "standard rate" of 45 per cent. In 1948, the first £50 was to continue to be taxed at 15 per cent, but the 30 per cent rate was to apply to the following £200 before the standard rate of 45 per cent applied. It was estimated that these changes would relieve some 500,000 low-paid workers of all income tax payments and lower the payments considerably for many others. On the other hand, surtax rates were to continue as before, running from 10 to 52.5 per cent, and any income affected by the maximum rate would be paying total income tax and surtax of 97.5 per cent.

Another tax development in 1948, which may be considered socialistic, was the imposition of the special levy on investment income. This tax, to be paid once and for all, applied only when the taxpayer's total income from all sources exceeded £2000 and his investment income exceeded £250. The rate of the tax rose from 10 per cent on the slice of investment income between £250 and £500 to 50 per cent on income exceeding £5000. Thus, the combination of the special levy and income taxes produced rates well over 100 per cent for certain amounts of investment income received by the extremely well-to-do. Again, the schedule of purchase taxes was revised and simplified. The maximum rate, on such articles as fur coats, was reduced from 125 to 100 per cent of the wholesale price. Other rates used were 66.7 and 33.3 per cent. There were reductions in the purchase tax on some household goods, and increases on high-grade clothes, furniture, furnishings, and other items. Higher excise taxes on tobacco products and on beer, wines, and spirits were probably due to causes other than the general socialistic philosophy of the government.

*The Public Debt.* The public debt of the national government of Britain amounted to £8,144,000,000 in 1938. During World War II it increased sharply and reached £24,453,000,000 in 1946.<sup>18</sup> While

<sup>18</sup> *The Economic Almanac for 1946-47*, p. 353.

this represented a tripling of the debt, the increase was much smaller than that which occurred in the United States and elsewhere. The Labor Government did nothing very important in connection with the public debt between 1945 and 1948 and probably will not in the future. The debt is looked on as a rather permanent phenomenon in Britain, and people in general do not look to the government to pay off its principal sum. Britain's economic situation since the war would probably have kept the government from making any very serious inroads in the debt in any case.

### *Public Finance under Fascism*

**Public Expenditures** The Italian government under fascism was not the owner and operator of all or most Italian industries and businesses. Rather, as under capitalism, the activities of government were superimposed on an economy in which the bulk of economic activity was in the hands of private individuals and firms. In the early years of fascism therefore, the government performed just about the same functions that we should expect the government of any capitalistic economy to perform. The budget was balanced and the heavy deficits of the war and early postwar years were replaced by moderate surpluses in the fiscal years from 1924 to 1930. In this general era of prosperity, taxes on landed property and business were lightened, real estate assessments were revised, and the inheritance tax was abolished. The tax base was broadened and increased direct and indirect levies were placed on the incomes of urban and rural workers.

After 1930, the expenditures of the Italian government increased moderately during the great depression, somewhat more during the war with Ethiopia, and very sharply indeed as Italy prepared for and participated in World War II. That is, governmental expenditures amounted to 19.6 billion lire in 1929, 23.2 billion lire in 1932, 33.1 billion lire in 1936, and 96 billion lire in 1941. The chief items of expenditure in the depression years were various governmental aids to business, national defense, and interest on the public debt. Later on, national defense came to absorb an ever increasing part of total governmental expenditures. From 1936 through 1944, expenditures for national defense and war amounted to approximately 400 billion lire, or about 57 per cent of total expenditures of 709 billion lire. Total governmental expenditures in 1943, the last year

of the war for Italy, constituted about 80 per cent of total national income.<sup>19</sup>

In the fiscal year ending March 31, 1934, the first full year after the National Socialist Party came into power, the total expenditures of the German government amounted to 9.7 billion marks. They had increased to 25 billion marks by 1938. In the fiscal years from April, 1939 to March, 1945, the German government spent a total of 687 billion marks, or an average of 114.5 billion marks per year. Depression expenditures were important only in the very early years of the fascist regime. In the years just before World War II, about two-thirds of total governmental expenditures were for national defense, and war expenditures amounted to 80 per cent of the total in the fiscal year 1945. For the period 1939-45, about 75 per cent of total expenditures on the average, or a total of 514 billion marks, were for war.<sup>20</sup>

**Public Revenues** The revenues of the Italian government declined from 20.2 billion lire in 1929 to 18.1 billion lire in 1934, and then increased gradually until a peak of 48.9 billion lire was reached in 1943. From 1932 through 1943, governmental revenues fell well short of expenditures. In 1932 some 60 per cent of total revenues came from direct and indirect taxes on consumption, while the income tax yielded only about 20 per cent of total revenues and had the added disadvantages of beginning with very small incomes and providing comparatively low rates in the higher brackets.<sup>21</sup> Later in the 1930's, increased revenues depended on higher taxes on consumption, a newly introduced sales tax, and capital levies on the value of real estate, the capital and surplus of corporations, and the capital of unincorporated enterprises.

From 1936 through 1944, governmental revenues amounted to 306 billion lire, or almost exactly enough to cover the non-war expenditures of the period,<sup>22</sup> with the cost of the war being carried "on the cuff." During the years of Italy's participation in World War II, direct taxes were producing less than a quarter of total revenues, while profits of governmental monopolies (tobacco, salt, quinine, public lotteries, matches, automatic lighters, and cigarette papers)

<sup>19</sup> *Fascism in Action*, p. 66

<sup>20</sup> *Ibid.*, p. 64

<sup>21</sup> C. T. Schmidt, *The Corporate State in Action*, pp. 128-129

<sup>22</sup> *Fascism in Action*, p. 66

produced from one-seventh to one-fifth of the total. The rest came from a host of other taxes, licenses, and fees. In 1943, direct taxes yielded 10.8 billion lire, governmental monopolies 8.9 billion lire, and all the other taxes 17.5 billion lire, out of total revenues of 48.9 billion lire.<sup>23</sup>

The Italian income tax was of a rather peculiar character. Income was classified according to the sources from which it was derived, and then flat rates of tax were applied to taxable income, regardless of amount, in the various classifications. A supplementary tax was levied on family incomes at moderately progressive rates. Inheritance tax rates, on amounts above the exemptions granted, varied from 1 to 50 per cent depending upon the degree of relationship between the decedent and his heirs, the size of the inheritances, the age and civil status of the decedent and the heirs, and other factors. Transfers between parents and two or more of their children were completely exempt from inheritance taxes. Excise taxes were high, and the high prices charged by governmental monopolies yielded large profits. The system as a whole seems to have been highly regressive in character.<sup>24</sup>

Ordinary revenues of the German government increased from 6.6 billion marks in 1933 to 17.7 billion marks in 1939 and 44.1 billion marks in 1943, before declining moderately in 1944 and 1945. Other receipts, including such items as war contributions from states and communities and occupation costs assessed on occupied territories, increased rapidly from 4.5 billion marks in 1940 to 37 billion marks in 1944.<sup>25</sup> Total revenues fell well short of total expenditures in all the years of the fascist regime. In the early years, income taxes produced about one-fifth of all tax revenues. This proportion grew to one-fourth and, at the end of World War II, to more than one-third. Taxes on corporate incomes grew from almost nothing to nearly one-fourth of total tax revenues. The turnover tax produced from one-sixth to one-fifth of the total over the whole period, and customs duties and excise taxes, which produced more than one-third of all tax revenues in 1933, declined to a point where they yielded about one-fifth of the total.<sup>26</sup>

The amount of income tax an individual paid depended upon the size of his income, the number of his children, and whether or

<sup>23</sup> *Ibid.*

<sup>25</sup> *Ibid.*, pp. 64-65

<sup>24</sup> *Ibid.*, pp. 70-71

<sup>26</sup> *Ibid.*, p. 64

not he was a Jew. In 1943, the effective rates for unmarried persons began at 1 per cent on an annual income of 600 marks and increased to 66 per cent on an income of 135,700 marks. On the other hand, the rates for persons with five children began at 0.3 per cent on an income of 4000 marks and increased to 56 per cent on one of 135,700 marks. The corporation income tax had been levied at the rate of 20 per cent before 1936, was increased to 35 per cent for 1938, and thereafter amounted to 40 per cent. An excess profits tax was levied in 1942 at the rate of 25 per cent for individuals and 30 per cent for corporations on all incomes above an exemption which could be calculated on any one of five alternative bases.<sup>27</sup>

Inheritance taxes in Germany ran from 2 to 60 per cent according to the amount of the inheritance and the degree of relationship between decedent and heirs. The tax rates applied to all inheritances above certain exemptions which themselves varied on the basis of degree of relationship. The general property tax of the central government amounted to 0.5 per cent on the value of all property above rather liberal exemptions. The turnover tax was based on gross receipts from the sale of goods and services. It applied to about four-fifths of all transactions and was levied at a rate of 2 per cent in the case of about three-fourths of the taxed turnovers. Finally, excise taxes were applied to many products, such as tobacco and products, alcoholic beverages, salt, sugar, saccharine, mineral oils, illuminants, matches, playing cards, and amusements.<sup>28</sup>

*The Public Debt.* With public expenditures exceeding revenues by considerable amounts, the national debts of Italy and Germany grew rapidly. The fascist regime in Italy inherited a debt of 95 billion lire and had increased it to about 134 billion lire by 1938. In later years, with revenues covering only non-war expenditures, the debt expanded immensely and amounted to over one trillion lire in two years after the end of World War II.<sup>29</sup> In 1938, four-fifths of the debt had been represented by government bonds but after the war about four-fifths of it was unfunded or floating.

In Germany, the national debt increased from 12 billion marks in 1934 to 34 billion in 1939 and 473 billion at the end of World War II. Both long-term obligations and a great variety of short-term obligations were issued by the government, but about four-fifths of all

<sup>27</sup> *Ibid.*, pp. 67-68.

<sup>28</sup> *Ibid.*, pp. 68-69.

<sup>29</sup> *Ibid.*, p. 73.

borrowing was short term toward the end of the war.<sup>20</sup> The government borrowed heavily from the central bank and from the commercial and savings banks of the country. All through the war, the general public was not asked to subscribe to a war loan. However, the government did borrow directly from productive enterprises, by using such things as tax credit certificates and delivery bills in paying for purchases, and from wage earners through the so called non-savings plan. Workers could specify that certain numbers of marks should be deducted directly from their earnings in each pay period and placed to their account in credit institutions where they would be accessible to the government. Tax reductions were granted on these iron savings, but they were not to be withdrawn until after the war and even then only on a year's notice.

The continued excess of public expenditures over revenues and the rapidly growing debts of the fascist governments might have been considered dangerous according to prewar capitalistic standards, but they were not likely to lead to economic breakdowns in the closely controlled economies of Italy and Germany. So long as productive facilities, workers, and necessary materials and resources were available, the fascist economies were likely to continue to function about as well as usual under the strict supervision of the government regardless of the size of the national debt or the lack of balance between public expenditures and revenues.

#### QUESTIONS

- 1 "The functions which are performed collectively through the government under capitalism rather than by individuals are of several general kinds." Explain.
- 2 "The functions of government under capitalism are to be regarded as a means of overcoming to some extent the deficiencies of the capitalistic market and price mechanisms." Show whether you agree.
- 3 What general principle can you suggest for deciding the number and kinds of functions to be delegated to government under capitalism? Explain.
- 4 "Several economic principles are available for the guidance of government in setting up a sound system of taxes in a capitalistic economy" Explain.
- 5 Why have the expenditures of all types of governmental units in the United States increased so greatly in recent decades? Explain.

<sup>20</sup> *Ibid.*, pp. 72-73.

- 6 How did the great depression following 1929 affect governmental functions and expenditures in the United States? Explain
- 7 Can the functions and expenditures of our various governmental units be justified on the basis of the criterion proposed in the text? Explain
- 8 Comment on the necessity for the principal depression expenditures of our federal government during the 1930's, in the light of the suggested test for public expenditures
- 9 Describe and evaluate the activities and expenditures which are proposed for the federal government of the United States in the postwar period
- 10 "On the whole, taxation in the United States does not conform satisfactorily to the principle of ability to pay" Do you agree? Explain
- 11 Is it true that the public debt of the United States government is certain to be burdenless in the future because "we owe it to ourselves"? Explain
- 12 "There can be no sound objection to financing governmental expenditures through public borrowing" Discuss
- 13 "Even in ordinary times, the expenditures of a socialistic government would bulk very large in relation to national income" Explain
- 14 "Whether a socialistic government would need to levy any taxes would depend on the manner in which the leaders decided to operate the economic system" Show whether you agree
- 15 "An unbalanced budget would mean comparatively little in a socialist economy" Do you agree? Explain
- 16 Indicate the chief items of expenditure of the federal government of Soviet Russia
- 17 "The sales or turnover tax is not open to as serious objections in the socialized economy of Soviet Russia as in capitalistic countries" Show whether you agree
- 18 Criticize the turnover tax employed by the government of Soviet Russia
- 19 "Direct taxes on individuals play a rather unimportant part in the Soviet revenue system" Explain
- 20 Discuss the Soviet Russian policy with respect to public borrowing
- 21 What has happened to public expenditures and revenues in Britain under partial socialism? Explain
- 22 "Recent changes in the British tax system indicate the socialistic philosophy of the Labor Government" Do you agree? Explain
- 23 "Fascist public finances followed the same pattern in both Italy and Germany" Show whether you agree
- 24 How did the tax systems of the fascist countries differ from those of the United States and England during World War II? Explain
- 25 "The size of the public debts of the German and Italian governments was relatively unimportant under fascism" Explain

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CHAPTER 22

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## *EVALUATION OF CAPITALISM*

HAVING completed our discussion of several important individual phases of economic activity in the various economic systems, we shall now attempt to summarize the points of strength and weakness of these systems and evaluate each system as a whole. The task of evaluation is extremely complicated. Every economic system has some strong points and some weaknesses, some advantages and some disadvantages, and a general opinion of approval or disapproval can be reached only by balancing the favorable and unfavorable processes and results against each other in some way. No economic system is so satisfactory that all its methods and results can be given unqualified approval.

In evaluating an economic system, it is difficult to concentrate attention entirely on economic processes and results and yet the consideration of the noneconomic institutions and processes would further complicate the task of evaluation. If an economic system has greatly increased production and the standards of living of its people and at the same time has acquired a strong dictatorial government which strictly regiments the activities of the people, how and to what extent shall we balance one of these factors against the other? If an economic system has greatly enlarged its educational activities, increased the literacy of its people, and improved the position of women, but at the same time has severely limited the religious activities of the people and weakened the family as a social institution, how shall we balance these results against each other and how shall we relate them to the economic accomplishments and failures of the system? Many other kinds of men besides "economic men" inhabit the bodies of most individuals, and there are many people who regard the strictly economic accomplishments of a country as virtually worthless if they are accompanied by the de-

struction of religious liberty or the establishment of a nondemocratic government.

The process of evaluation is made still more difficult by the fact that some economic systems which we are studying are very young or had only short careers. The Soviet Russian economy has been operating only 30 years, and it has been functioning under economic planning only 20 years. The Italian economy operated only about 21 years, and the German economy only about 12 years, under fascism. Partial socialism in England is in its fourth year. On the other hand, the capitalistic system of the United States has been operating independently for 160 years. It is usually difficult, in the early years of an economy, to see exactly what it will be like after many years of development, and there is no completely satisfactory method of comparing what one economic system has accomplished in a few years with what another economy has accomplished over a much longer period of time.

If a particular type of economic system operating in a certain country produces some noteworthy accomplishments and some conspicuous failings, it is a trying task to separate those results which may be attributed to the type of economic system operated from those which have been due to a variety of natural and other factors which would have conditioned the operation of any kind of economic system in the given country. If the economy of the United States is deemed to have operated successfully under capitalism, what part of its success has been due to the existence of the capitalistic system in the country and what part to the large quantities of fertile land, abundant natural resources, and relatively sparse population which might have insured that almost any kind of economic system would have operated in the country with at least fair success? What part of the results achieved by the Soviet Russian economy can we attribute to socialism itself, and what part has been the product of various peculiarities of the Russian situation? Perhaps socialism would have a much better (or much worse) chance to succeed in Great Britain or the United States.

It is far from completely satisfactory to try to compare and evaluate economic systems only in general terms, and yet it is frequently true that important types of statistical data are either unavailable or of questionable value. The governments of some of the countries which we are studying either have not had or have not cared to publish statistical data on certain vital economic matters.

Even when they have issued statistics on certain points, they may have put out only the favorable data and suppressed the rest, or they may have exaggerated or altered the figures in order to give a favorable impression of the economic results which they have achieved. As a result, in comparing and evaluating economic systems, we should ordinarily use statistical data only to gain general impressions of accomplishment rather than for precise comparisons.

A final difficulty in evaluating economic systems is found in the fact that we lack generally acceptable standards of evaluation. Even if we had adequate statistical data, if all economies were directly comparable, if we could gather together and bear in mind all the complex attributes of the economies, and if we could exclude or appropriately include various noneconomic aspects, we should still not know whether the results produced by the various economies were good or bad unless we had decided what results should be considered good or bad for an economic system. Many persons attempt to evaluate other economic systems by attributing to them the same goals or objectives which are deemed appropriate for the United States, and by considering other economies successful if they achieve these objectives or unsuccessful if they fail to achieve them. This method is not entirely valid, for different economies may have somewhat different objectives. Clearly, it is not altogether fair to criticize a person for not winning a contest in which he is not even entered, or to criticize an economy for not achieving a result which was no part of its intention. We should not condemn an economy as inefficient because it produces a low standard of living for its people, unless we have reason to think that it is trying to produce a high standard of living in the period in question. In other words, we should try to relate the methods and results of each economy to its own goals and objectives, although there may be no harm in pointing out, where it is true, that the objectives sought by some economies are repugnant from the point of view of our own ethical standards.

### *The Accomplishments of Capitalism*

**Production under Capitalism** With these difficulties in mind, we proceed to the evaluation of various economic systems, starting with capitalism. Since there are some differences from one capitalistic system to another, our arguments will be particularly concerned with

the capitalistic system of the United States Our evaluation of production under capitalism will deal with two questions (1) How successfully does the system adapt its productive activities to basic human needs and desires, or, in other words, does the system set out to produce the things that its people want? (2) Once decisions have been made, for better or worse, as to the things which should be produced, how efficiently does the system operate in producing these things?

With regard to the first of these matters, it is quite possible to reach a conclusion favorable to the capitalistic system Its method of adapting production to basic human needs and desires is to leave private enterprisers free to respond, on the basis of costs, to the prices which people are able and willing to pay for commodities and services in the market Now there is no doubt concerning the willingness and ability of producers to respond to prices in the market One can get almost anything produced if he is able and willing to pay enough for it Neither is there much doubt concerning the ability of prices, in and of themselves, to serve as a medium for expressing the relative strength of human desires for many commodities and services

The chief problem seems to be whether various individuals are capable of using prices effectively as a means of expressing their needs and desires In a capitalistic system in which individuals have widely varying amounts of money income to use in offering and paying prices and also have some needs and wants which cannot be well expressed in terms of prices in the market, it is too much to expect anything approaching perfection in this matter And if prices do not express accurately the relative strength of various human needs and desires, then even a complete adaptation of production to prices in the market will not give us a perfect adaptation of production to these needs and desires Nevertheless, the results achieved by capitalism in this matter may compare favorably with those which can be attained by any alternative method, as, for example, by economic planning

We should also note briefly here that the capitalistic system achieves reasonably good results in this matter while affording the individuals of the system a rather high degree of personal freedom It is undoubtedly a mistake to think of economic freedom, as some people do, solely as a means of accomplishing certain results It is a means to other ends, of course, but it is also an end in itself, and one

which is greatly desired by large numbers of people. And there is a serious question whether some economic system other than capitalism could do better in the matter of adapting production to human needs and desires for commodities and services without, in the process, placing severe limitations on the economic freedom of its people, and perhaps on their political freedom as well.

Turning now to the other question of efficiency in production, we find that there are many things to be said in favor of capitalism. One of the chief accomplishments of our capitalistic system is found in its tremendous expansion of production and of economic activities in general through time. Many of our industries today have outputs which are many times (in some cases, hundreds of times) as great as those of several decades ago, and other industries produce great volumes of commodities today which were not being produced at all a few decades ago. In view of the fact that, over most of the life of our capitalistic system to date, the outstanding economic problem has been that of a general shortage of all kinds of commodities and services, this accomplishment in the field of production is not to be taken lightly. Even the severest critics of capitalism admit the desirability of the accomplishments of our system over most of its life. Capitalism, so it is said, revolutionized the operation of industry and agriculture, modernized the backward countries, and increased the volume of international trade. The aim of the capitalistic system was the maximization of output. It tried to expand and cheapen production rather than to restrict it. Business depressions slowed up progress in production only temporarily and, while technological changes threw people out of work at times, the rapidly expanding economic system quickly and easily reabsorbed them.

This reference to technological change is pertinent. Our capitalistic system did not increase production merely by using larger quantities of the various productive agents. That would have been a relatively easy accomplishment. Instead, constantly improving machines and methods of production have made it possible for given quantities of the productive agents to turn out larger and larger quantities of economic goods of all kinds. While the rapid technological change which has occurred in our economy must be attributed to the character and ability of its people as well as to the existence of the capitalistic system itself, the system played its part in the development by affording almost boundless opportunities for

economic gain to the successful innovators The principles and methods of capitalism in the field of production have been so efficient and successful that they are used even today in all types of economic systems Formerly capitalistic economies may turn, for various reasons, to socialism or fascism, but their productive activities continue to be specialized, roundabout, and large scale, as they were under capitalism, and these economies develop or continue to have vertical and horizontal combinations of productive establishments comparable to those which exist in our capitalistic economy

*Standards of Living* The great increases which have taken place in production in our capitalistic system have brought improved standards of living to the individual citizens The improved standards of living have included not only larger quantities of goods formerly consumed but also an ever-increasing variety of commodities and services The gains in living standards have been shared by all classes of citizens, by wage earners as well as by enterprisers, capitalists, and landowners Real wages, for example, as of the year 1900 were probably at least twice as great as they had been a century before While it cannot be said that the gains from increased production have been shared at all equally by the various economic classes of citizens and while it may be true that the gulf between the incomes and standards of living of the rich and those of the poor has expanded instead of diminishing over the years, it cannot be denied that all general classes of citizens have gained as the result of the increasing productivity of our capitalistic system

*The Distribution of Income* Everyone knows that the distribution of income in our capitalistic system is highly unequal as between individuals and families Moreover, as we have seen and shall note again, many unfortunate results flow from this great inequality in the distribution of income However, it is quite possible for the ardent supporters of capitalism to make a case for the capitalistic distribution of income among persons and families, unequal as it is In the first place, this inequality is the result of the more or less automatic operation of the price system, which sets high prices on scarce and highly productive factors of production and low prices on more plentiful and relatively unproductive factors of production Such high and low prices for various grades of productive agents give large and small incomes respectively to the owners of these agents Since the rational use and allocation of the productive

agents depend upon these market-determined prices for the agents, it is difficult to see how our capitalistic system could operate on the basis of the price mechanism without producing considerable inter-personal and inter-family inequalities in the distribution of income.

In the second place, many people argue that the inequality in the distribution of income which is produced more or less automatically by the operation of the price system under capitalism is desirable in itself. In the absence of perfect knowledge as to what human nature is like, ardent supporters of capitalism are inclined to think that most people have a selfish and acquisitive element in their natures and that the capitalistic system is more efficient and productive than any other, precisely because it caters to the acquisitive urge of the people. If people are naturally acquisitive, nothing is so likely to stimulate them to great industry and efficiency, to improvement and innovation, as the ability or opportunity to secure large economic gains as the reward for conspicuous accomplishments, and any economic system which intends to eliminate or severely limit differential incomes and replace economic motivation with incentives of other types is doomed from the start to inefficiency and stagnation.

These conclusions concerning economic motivation are highly controversial and many critics of capitalism would object to them strongly. However, observation of our capitalistic system in operation indicates that most of the people in most of their economic activities are motivated more strongly by the desire for economic gain than by anything else. To what extent the acquisitive behavior of people under capitalism is natural and to what extent it is the product of the capitalistic institutional environment is an oft-debated question, but there is no noncapitalistic system in actual operation today which furnishes completely convincing evidence that other types of incentives can be entirely and effectively substituted for the economic under any institutional set-up. To be sure, differences in incomes in Soviet Russia are much smaller, at least before taxation, than in our capitalistic system, but this will not indicate anything definite about the effectiveness of other incentives unless and until the efficiency and productivity of the Russian citizens approaches that of our own.

It is also sometimes argued that great inequality in the distribution of income, as it exists under capitalism, is desirable because it provides a situation that is ideal for that rapid and continuous

accumulation of capital funds which is so necessary to an efficient and progressive economy As one writer puts it,

The thesis is that there is one way, and only one way, that any people, in all history, have ever risen from barbarism and poverty to affluence and culture, and that is by that concentrated and highly organized system of production and exchange that we call Capitalistic, one way, and one alone Further that it is solely by the accumulation (and concentration) of this Capital, and directly proportional to the amount of this accumulation, that the modern industrial nations have arisen This accumulation of what we term wealth is largely the achievement of a relatively few individuals, gifted, for this special purpose, far beyond their fellows and their time In all ages, great merchants and traders, great enterprisers

And this wealth is not, as almost all the earlier economists assumed, the product of "labor", nine-tenths of it is directly the product of *machines*, these and these alone made possible the present-day colossal aggregate of Capital<sup>1</sup>

And what is the method, or mechanism, by which all this vast system of production and transportation has been created? Virtually, by placing this surplus, this capital accumulation, largely in the hands of a relatively few individuals, with rare gifts for the management and utilization of this surplus, all for the general good The price—the reward to the rich and exceptionally capable! A bagatelle The actual "consumption," or expenditures of the three or four per cent of the population whom we class as "rich," is so slight as to be of no practical importance All the rest of the income of this slender class is immediately turned back into industry, for the development of the country and for higher standards of living which an immensely larger part of the population now enjoys

Deep is the prejudice against avarice, and thirst for gain And yet they are literally the most beneficent forces in modern society Because the only possible way that this desire for gain and accumulation, and the profit system can be most effectively realized and advanced, is by the increase in the comforts and enjoyments of the whole population, or at least of by far the larger part<sup>2</sup>

And even the underprivileged are better off than ever before

According to this opinion, an economy which is to be prosperous, efficient, and progressive must make widespread use of roundabout and large-scale methods of production, but these productive methods require large amounts of capital If the national income were equally divided among the citizens, comparatively little saving would occur It is estimated that 70 per cent of the people do no saving, and that the redistribution of the savings of the rich would

<sup>1</sup> Carl Snyder, *Capitalism the Creator* New York The Macmillan Company, 1940, pp 4-6 Reprinted by permission of the publishers

<sup>2</sup> *Ibid.*, pp 7-8 Reprinted by permission of the publishers

give each of the gainfully employed in our economy an additional monthly income of only about \$5, which almost certainly would not be saved.<sup>3</sup> We must depend upon the incomes of the relatively few people of great wealth, and especially on the reinvestment of profits in industry, for the necessary saving and capital formation. In this situation, it is fortunate that there is great inequality in the distribution of income under capitalism, and that wealth and income are concentrated in the hands of a relatively small number of people for

the larger the wealth and income of these few individuals, the greater the proportion of profits that is turned back into industry, for industrial expansion and for the creation of new industries. As the margin of net profit is small and precarious, whatever tends to limit profits or to reduce them is imminent to the continued growth of the country and opposed to the best interest of the whole population. Finally, as the highest rate of savings is from the largest fortunes, it follows that until we can devise a more efficient system, the greater the concentration of income the greater the capital supply, and therefore, the greater the gain in national well-being.<sup>4</sup>

It also appears to be true, according to this line of argument, that there is substantial harmony between the interests of the great masses of workers and those of the relatively few individuals who receive large incomes. The rich prosper only by benefiting the masses and by adding to the comforts and enjoyments of virtually the whole population, while the wages and standards of living of the workers are higher than they would be otherwise because of the activities of the rich in saving and investing large portions of their incomes.

The average wage paid per wage earner has risen steadily and proportionately, with the "value added" and with the physical volume of manufactures. The ratio of wages to the total value of product has not materially changed in the last eighty years. The entire increase in average wage per wage earner, or in real wages, has been due directly to one factor and to one alone—the growth in capital investment. This must be so, because wages are paid out of product, and the larger product per worker has been wholly due to the increased application of machinery. The increase in mechanical equipment was possible only because of the increase in the supply of capital. Therefore, the well being of the great body of workers has been improved solely through the provision of an adequate supply of capital for investment.<sup>5</sup>

<sup>3</sup> *Ibid.*, p. 143.

<sup>4</sup> *Ibid.*, p. 125. Reprinted by permission of the publishers.

<sup>5</sup> *Ibid.*, p. 127. Reprinted by permission of the publishers.

Thus it seems that wages are not influenced by custom, bargaining power, cost of living, the capitalist or employer, the wage earner or labor union, sentiment or law. They depend upon the average product per worker—a function of the amount of capital and the stage of mechanical development.<sup>6</sup> Moreover,

If higher wages come solely from increased production, if increased production comes solely from additional capital, and if this capital is derived almost wholly from profits, it must follow that the highest rate of profits will promote the greatest progress and increase of wages.<sup>7</sup>

From this point of view, it is not difficult to conclude that the people who do not make out very well under capitalism and who are not satisfied with the way in which the system operates are the incapable, the inefficient, the morons, and the derelicts.<sup>8</sup> These ne'er-do-wells realize that their income status is unsatisfactory, and they are unwilling to believe that the difficulty may lie within themselves. Therefore, they blame the capitalistic system for their troubles and naively imagine that they would be much better off under some other system. It is also easy to conclude from this point of view that the enactment of legislation or the formation of labor unions for the purpose of raising the wages and improving the economic status of the workers is somewhat unfortunate. Since increasing wages through time depend upon the large incomes and savings of the owners and managers of industry, attempts to get higher wages in the present by forcing owners and managers in effect to share their incomes with the workers tend to kill the goose that lays the golden eggs.

*Freedom and Automaticity* At this point we may note in greater detail than formerly that our capitalistic economy is credited with providing a great degree of political and economic freedom for the individual citizens. In the minds of many people, capitalism is a synonym for democracy, while socialism or fascism inevitably implies dictatorship. In practice, of course, neither the government of the United States nor that of any other capitalistic country is necessarily qualified to serve as a model of political democracy, but the fact remains that in the past the only semblances of democratic government worthy of the name have been found in countries which also operated under capitalism. It is true that modern socialists, in

<sup>6</sup> *Ibid.*, p. 168

<sup>7</sup> *Ibid.*, p. 143 Reprinted by permission of the publishers

<sup>8</sup> *Ibid.*, p. 8

describing the conditions which would prevail in their ideal system, contend that the government would be highly democratic in character, but in this matter we may well hold that "seeing is believing," for the governments of all actually operating noncapitalistic systems, whether socialistic or otherwise, have been essentially dictatorial and undemocratic. What the government of Great Britain will be like, when its socialistic system has had more time to develop, remains to be seen.

The individual also enjoys a great measure of economic freedom in our capitalistic system. Except in the case of activities which are deemed undesirable by common consent, he is free to pursue his own ends in his own ways. He is free to become a business enterpriser in any type of business or field of economic activity which appeals to him, or, if he is unable to strike out for himself, he may at least choose freely among all the occupations for which he is qualified. However great the amount of wealth and income which he may acquire by legitimate means, he may be sure that he will be protected in its use and enjoyment. There is no legal limit on the degree of economic advancement which he may attain. While he is limited by various environmental conditions and by his own talents and abilities, it is perfectly possible for him to start his economic career poor and insignificant and to end it rich and influential. And he may pass his wealth on to his heirs, subject to taxes which are imposed by various governmental units.

Since these conditions prevail for individuals, it may be said that our capitalistic economy as a whole operates freely and automatically. No individual or small board or commission of individuals is clothed with the power to determine the kinds and quantities of economic goods which are to be produced in the system, the way in which the various productive agents are to be allocated or distributed among the various industries and fields of productive activity, the manner in which the immediately available stocks of consumers' goods are to be distributed among consumers, and the total quantity of each reproducible agent of production which is to be available in the long run. Decisions on all these important economic matters are made by individuals, to be sure, but by large numbers of individuals and on the basis of price relationships rather than on the basis of arbitrary authority. The total decisions on all these points are merely the aggregate of the decisions which individuals make on the basis of price relationships, and our capitalistic economy is pre-

pared, in general, to accept the total economic results produced by these decisions as good, not because they are necessarily more nearly perfect than any other results which could be produced but because they are produced freely and automatically.

Moreover, it may be argued that our capitalistic system, besides working freely and automatically, does operate on the whole to furnish the individual citizens with the kinds and quantities of economic goods which they desire, in so far as the prices which individuals are willing and able to pay for various goods on the market give a true indication of their basic desires. And the capitalistic system is flexible, in that its productive activities adjust themselves rather quickly and precisely to the changing desires of consumers as expressed through the price mechanism. It is doubtful if any economic system which operates on the basis of governmental control or economic planning can be as flexible as the capitalistic system. On the other hand, it is possible for the government of our capitalistic system to step in with needed restrictions and reforms in cases in which the results produced by the automatic operation of the system are in part unacceptable to the citizens as a whole. Even the critics of our system admit that it is possible for our government to achieve some redistribution of wealth and income through taxation, to reduce the cultural gap between different levels of the population, and to improve living standards for the underprivileged. The activities of government have not made our capitalistic system perfect, but they have kept many people from starving and from living under what the socialists call conditions of revolting and brutalizing poverty, misery, and destitution.

The recurrence of severe business depressions also injects a highly discordant note into the general melody of automaticity and flexibility under capitalism. However satisfactory or unsatisfactory the results produced by our capitalistic system when operating at full blast may be, the fact remains that it is subject to these periodic breakdowns or depressions and that these breakdowns produce a host of unfortunate results in terms of unemployment for millions of workers, the failure of thousands of banks and business concerns, and warehouses groaning with stocks of goods while the wants of millions of consumers clamor for satisfaction. However, the ardent supporters of capitalism claim that, in their expanding and progressive economy, business depressions slow activities down only temporarily and are to be regarded as a kind of "growing pains."

They contend further that business depressions are not inherent in the nature of the capitalistic economy as such. In some cases, they regard depressions as due to the operation of factors which we have not yet subjugated but may some day bring under control. Thus, some people consider depressions to be caused wholly or largely by the overexpansion of bank credit and accompanying wild speculation—factors which may be eliminated readily by the development of wise banking policy. In other cases, depressions are attributed to more or less uncontrollable factors, but it is contended that these same factors would remain uncontrollable in any type of economic system. If depressions are the result of the mistakes that are made in producing on a roundabout and large-scale basis in anticipation of demand, the same difficulties would be encountered in any economy which did not wish to give up these methods of production.

### *Failures and Weaknesses of Capitalism*

**Adapting Production to Human Needs and Desires** The chief criticisms of our capitalistic system, in connection with adapting production to basic human needs and desires, center around three points. In the first place, it is held that prices in the market do not measure accurately either the needs and desires of the citizens as consumers or the real costs of production. Inequality in the distribution of income is the factor which keeps prices from indicating accurately the relative strength of the citizens' desires for various commodities and services. It makes the critics' blood boil to see a rich family with its 50 automobiles while poor people cannot even get shoes for their own transportation, to see the rich living in their million dollar mansions while the poor live in unbelievably squalid slums, and to see the rich lavishing mink coats and air-conditioned dog houses on their pets while the poor cannot command adequate amounts of food and clothing.

The behavior of capitalistic enterprisers in turning out luxuries for the rich before necessities for the poor is not necessarily illogical or uneconomic. It is simply wrong. If, on the basis of cost-price relationships, it is more profitable to produce luxuries and trivialities for the rich than to devote the same quantities of productive agents to turning out greater quantities of common necessities and comforts for the masses, capitalistic enterprisers as such cannot be blamed for the productive decisions which they actually make. The

fault lies with the tremendous inequality in the distribution of money income which makes it possible for the rich to offer higher and more profitable prices for luxuries and trivialities than persons of small income can offer for the ordinary necessities and comforts of life. The adaptation of production to prices in the market does not produce an accurate adaptation of production to human needs and desires under great inequality in the distribution of money income.

The point in connection with costs is that certain social costs may result from the operation of an industry or business and yet find no representation in the market. The operation of an enterprise may be injurious to the health of its workers. It may discharge wastes which pollute streams and kill fish, it may emit smoke, soot, and grime which will be costly to the citizens of the community in a variety of ways. Unwise consumption of its products may increase the costs of local government (as excessive use of liquor may require the employment of more policemen and judges). If enterprisers base productive decisions solely on the relations of prices and costs in the market, many articles may be produced and sold which would not be if the prices charged had to include the full social costs of production.

Having seen that some human needs and desires, and some costs, are not accurately represented by prices in the market, we now note again that some human desires cannot be expressed at all in terms of prices. The things most commonly mentioned in this connection are the negative preferences of the citizens and some of their more complex positive wants. In the market it is easy to bid for the things you want produced but impossible to bid against the things whose production you would like to see discontinued, except by refusing to buy. Similarly, the desire of people for greater social security or a higher level of public health cannot be readily expressed in terms of prices on the market.

These criticisms would be valid even if production under capitalism were always perfectly adjusted to prices in the market, but it is also true, of course, that this adjustment is never complete. Once agents of production are tied up in particular fields of production, it may be some time before enterprisers, even given the best of intentions, can adjust their production to the changed desires of consumers. Production is always in the process of getting adjusted to prices in the market, but full adjustment is never reached. For

all these reasons, the adaptation of production to basic human needs and desires is always far from perfect in our capitalistic system.

*The Efficiency of Production* The critics of our capitalistic system do not deny the great increases in the total volume of production which have occurred in the United States over the years. Neither do they deny that great technological progress has occurred nor that more efficient productive methods and principles have been developed. However, they do contend that our economic system is not nearly so productive as it should be. Some critics estimate that the productivity of our system is usually not over 50 per cent of what it might be, and that our national income in terms of commodities and services could be doubled or more than doubled without any increase occurring in the quantities of productive agents at our disposal.<sup>9</sup> Another estimate of a few years ago had it that the full use of available productive resources would provide the average family of four persons in this country with an income of \$4400 per year at 1929 prices.<sup>10</sup>

Just how far short of full efficiency our productive system falls may properly be a matter of dispute, but the events of recent years make it rather obvious that there is something wrong with our productive system as it ordinarily operates. After struggling along with a national income of 41.7 billion dollars in 1932 and one of 72.5 billion dollars in 1939, our economic system, under the stress of wartime conditions, passed a miracle and turned out a national income of 182 to 183 billion dollars in 1944 and 1945.<sup>11</sup> A part of this great increase in the national income was accounted for by the changing value of money and the rising general price level, but by far the greater part of it represented a genuine increase in physical production, even though many of the goods produced were not available or suitable for civilian consumption. Our citizens are surely entitled to wonder why, if our productive resources can be made to produce a large national income in wartime, they cannot be made to turn out a comparable volume of commodities and services with some regularity in times of peace.

<sup>9</sup> See, for example, Stuart Chase, *The Tragedy of Waste*. New York: The Macmillan Company, 1925, pp. 270-271, or E. Varga, *Two Systems*. New York: International Publishers, 1939, p. 51.

<sup>10</sup> National Survey of Potential Productive Capacity, *The Chart of Plenty*. New York: The Viking Press, 1935.

<sup>11</sup> W. N. Peach and W. Kruuse, *Basic Data of the American Economy*, p. 3.

*The Problem of Monopoly* The critics of our capitalistic system contend that the ineffectiveness of our productive system is due to many factors, one of which is the restriction of production and abuse of the profit motive by business enterprises with monopoly or quasi-monopoly powers Profits, which result from the disparity between prices and costs, are supposed to be a regulator of productive activity under capitalism Large positive profits in the production and sale of a particular economic good indicate that the output of that good needs to be expanded on the basis of effective demand in the market, and capitalistic enterprises, under the stimulus of these profits, are expected to expand output and, if necessary, then plant and productive facilities until the volume of the good which appears on the market is more adequate and the large profits are eliminated Conversely, the existence of negative profits, or losses, suggest that a certain economic good is currently being oversupplied on the basis of effective demand in the market, and the losses are expected to eliminate some enterprises and cause others to reduce their outputs until the market supply of the good is once more adjusted to the market demand and the losses are eliminated

Under this ideal operation of the productive system, positive profits appear as unimputable surplus income for the enterprises who receive them, but their temporary existence can be tolerated in view of the results which they produce In actual practice, however, many capitalistic enterprises have learned, according to the critics, that they can make more money by restricting output and charging high prices, even under relatively favorable market conditions, than they can by maximizing output That is, greater net incomes can often be obtained by producing and selling a small number of units of a good at a high price per unit than by producing and selling many units at a lower price per unit This seems to involve nothing more than the familiar principle that a firm which has any degree of monopoly control over the market for its product is likely to stop output at the point where marginal revenue is equal to marginal cost, instead of going on to the larger output at which price is equal to marginal cost

It is safe to conclude that such firms, other things being equal, will produce smaller outputs than firms in a strictly competitive situation However, since other things are not always equal by any means, we should not jump to the conclusion that we could reach an ideal situation by attempting to put down firms with varying

degrees of monopoly power. If, for example, the automobile industry had been in the hands of a thousand or so small competitive firms for the last few decades, instead of being largely controlled by a few great firms, it is far from certain that we should be getting today larger quantities than we do of better automobiles at lower prices. In some industries, production can best be carried on by rather large firms, and no one may think it worth while to organize such firms unless there is some assurance that a degree of control over the market can be attained, since otherwise the large necessary investment might be deemed too risky.

*Unused Capacity and Duplication of Facilities* According to the critics, our capitalistic productive system is less efficient than it should be because of a variety of so called competitive wastes. For example, there are large quantities of unused plant and equipment in our economy at most times. The idle productive capacity in 27 selected manufacturing industries in the United States ranged from 2 per cent in the manufacture of dairy products to 55 per cent in locomotive manufacture in 1929, according to a leading estimate. For manufacturing as a whole, unutilized productive capacity amounted to 17 per cent of the total in 1929 and averaged 20 per cent for the period from 1925 through 1929.<sup>12</sup> Even these figures are considered woeful underestimates by some critics because they are based on an extremely prosperous period, they leave out the productive capacities of enterprises which were completely idle in 1929, and they are based on "practical capacity" (or utilization usual under capitalistic conditions) rather than rated capacity. If the estimates of idle capacity are corrected for these factors, it is held that productive facilities in our manufacturing industries were actually utilized only to the extent of 50 to 57 per cent in the ten-year period from 1925 through 1934.<sup>13</sup>

Such idle capacity is often referred to as overcapacity or excess capacity, but it is not really excess capacity in the most fundamental sense, since all the goods which these idle productive facilities could have produced would probably have been eagerly consumed by the citizens. Of course, the great amount of idle capacity in the five years from 1929 through 1934 was the result of the great depression, but how can we account for large unused facilities in prosperous

<sup>12</sup> E. G. Nourse and associates, *America's Capacity to Produce* Washington: The Brookings Institution, 1934, p. 307.

<sup>13</sup> E. Vuga, *Two Systems* New York: International Publishers, 1939, pp. 46-51.

years? The common explanation is in terms of the competitive organization of industries. Each enterprise thinks that it has to be ready to handle not only its usual volume of business but also any business which it may succeed in getting away from its competitors. When each enterprise plans in this fashion, there tends to be idle productive capacity in the industry as a whole, and there is a tendency for competitive industries in general to "overshoot the mark."

Even when no productive facilities actually stand idle, there may be considerable duplication of facilities in a particular industry or business. Thus we often see a half dozen grocery stores struggling to get along in a small town where the entire volume of business could be handled by two stores, gasoline filling stations on all four corners of some busy intersections, and the wagons or trucks of a dozen dairies serving the same city block with milk and other products, with each vehicle stopping only at an occasional house. It is sometimes suggested that our entire needs for gasoline could be satisfied by one-third of the filling stations that we actually have and that there is an overinvestment of more than a billion dollars in this business. Idle productive capacity and duplication of productive facilities are closely related phases of the same problem, and both are often attributed to the competitive organization of industries and businesses in our capitalistic system. These factors also result in a waste of labor even in good times, although cyclical unemployment is the most important phase of the problem of idle labor.

*Undue Proliferation of Styles, Shapes, Sizes, and Colors of Goods*  
A second competitive waste is found in excessive varieties of goods, or what is called undue proliferation of styles, shapes, sizes, and colors. In the United States some years ago, if a man wanted to build a brick house, he could have his choice of 75 kinds of face brick and 44 kinds of common brick. If, in the spring, he wanted to do a little painting, he could choose from 480 varieties of paint and varnish brushes. If he wanted a new roof on his house, there were 60 kinds of roofing slate. For fencing in his yard, he could choose from 552 varieties of woven wire fencing. For his home workshop, he could select from among 1351 kinds of files and rasps. There were 441 varieties of staple vitreous china plumbing fixtures for bringing the bathroom up to date. He could wear some one of 36,845 varieties of men's hats and one of 278,000 varieties of men's suits. He could use any one of 42,877 kinds of solid section steel windows in

constructing his factory, and do his chopping with some one of 991,840 varieties of axes. Finally, if he wearied from all these activities, he could rest on any one of 78 varieties of beds, springs, and mattresses.<sup>14</sup>

Many things can be said about this problem. No one wants to eliminate variety entirely. A reasonable number of varieties of each kind of goods would be desirable in any economic system. Much can be done and has been done about the problem of undue proliferation even within our traditional capitalistic system. However, undue proliferation is admittedly wasteful, for large quantities of a few varieties of goods can almost always be produced more cheaply than small quantities of a large number of varieties. Finally, undue proliferation is attributed very largely to the efforts of competing enterprises to sell their goods and gain customers. It would not be expected to be much of a problem if each industry were operated by a private monopoly or by the government.

*Wasteful Advertising.* Critics of our capitalistic system complain bitterly about the wastefulness of competitive advertising. Some advertising is approved as educational or informative, that is, it advises the consumer concerning new goods, new uses of old goods, or the times and places at which special bargains will be available. However, much of the advertising in our system is competitive or combative (some say nine-tenths of the total is of this variety) and is designed to sell one producer's variety of a particular good instead of another producer's brand. Advertising of this sort, if it does not increase the total sales of all the brands of a product and if consumers do not by chance derive greater satisfactions from the brands to which they shift than from those which they used to consume, is wasteful in that one producer's gain is another producer's loss. Such advertising may not be wasteful from the point of view of individual enterprises, for presumably one enterprise needs to advertise if other enterprises do, but from the broad social point of view it amounts to an unwise use of society's resources, according to the critics. If all gasoline, for example, were produced and sold by a governmental monopoly, there would be no reason for the industry to maintain as many closely similar brands as we now have and spend millions of dollars in advertising each brand.

<sup>14</sup> Most of these figures are from Stuart Chase, *The Tragedy of Waste*. New York: The Macmillan Company, 1925, pp. 168-169.

*Competitive Exploitation of Natural Resources* Finally, our capitalistic productive system is criticized for its wasteful competitive exploitation of natural resources In the case of bituminous coal, we have been told that, for every ton which we bring to the surface of the ground, another ton is left behind, forever beyond our reach This result has occurred because operators "cream the mines" by following the richest seams of coal and taking out only that which is readily accessible The mines are abandoned before the poorer seams are utilized, and eventually the roof of the mine collapses in many cases, so that the remaining coal, which once would have been merely difficult to take out, becomes practically impossible to obtain These results are attributed to the competitive organization of the industry That is, if one mine operator attempted to get out all the coal, while others continued to take out only the richest and most accessible seams, he would have higher costs of production than the competing enterprises and might well be forced out of business While creaming the mines may be a sound competitive practice, it is extremely wasteful from the social point of view

Competitive waste is also common in the exploitation of petroleum resources Because of peculiarities of geological formation, the oil in a particular underground pool does not seem to care whose well it goes up If one landowner in an oil field puts down a well and other neighboring landowners do not, he may be able to obtain not only the oil which lies under his land but also that which lies under his neighbors' lands Hence, the discovery of oil in a particular area has often been a signal for all landowners in the region to start drilling wells in the hope of getting the oil to the surface before others could capture it As a result, while one well for each eight acres of land is on the average most suitable for efficient exploitation, we have often had one well for each two acres of land and in some cases the wells have been so numerous that they often almost touched each other This matter of having too many wells has not only led to a wasteful duplication of productive facilities but has also been wasteful of oil The natural pressure which would otherwise have forced most of the oil to the surface has been dissipated, mechanical pumping of the oil has had to be undertaken at an early date, and oil sands have become flooded with water At one time, it was estimated that we were wasting three barrels of oil for every one we actually obtained However, in more modern times,

we have found ways to increase the effectiveness of exploitation in some of our newly discovered oil fields

Similar wastes, too numerous to discuss, have existed and still exist in the use of other natural resources, both those which are replaceable and those which are not. The waste of replaceable natural resources is not so serious as the waste of such resources as oil and coal which cannot be replaced, but it is important nevertheless. And these wastes are attributable very largely to the competitive exploitation of the resources. Most of them either would not exist or would be greatly minimized under social exploitation.

*Competitive Wastes and Monopolistic Wastes.* We should note in passing that the wastes which result from the abuse of the profit motive and those which result from the competitive organization of productive activity are to a great extent antithetical. We do not mean that both types of waste cannot exist at the same time in our economic system, but rather that the increase of one of these types of waste tends to diminish the importance of the other. For example, if all industries and businesses in our system were perfectly competitive, the wastes of competition might reach a maximum, but in that case there would be no abuse of the profit motive or restriction of production. That is, in a perfectly competitive industry, it is impossible for one enterprise to restrict production and raise prices, since he is producing exactly the same good as other enterprises and is too small a part of the industry to affect prices by his actions either in increasing or decreasing production. If he cuts his output in half, he merely receives the same price as ever per unit of product and has only half as many goods as formerly to sell. Since no one can get rich in this way, it is clear that it requires some degree of monopoly control in order to be able to abuse the profit motive by restricting output. On the other hand, if each industry or business were in the hands of a single monopolistic concern, there might be much restriction of output and abuse of the profit motive but there could be no truly competitive wastes. A monopolist might make mistakes in deciding upon the quantities of productive facilities which he should set up, but there would be no competitive duplication of facilities, no wasteful advertising of essentially similar competing brands, and no undue competitive proliferation of styles and varieties of goods.

Some of the wastes that are described as competitive do not really result from pure competition. If all enterprisers in an industry pro-

duce exactly the same economic goods so that the customer is perfectly indifferent as to which producer's goods he gets, there is no reason for any one enterprise to try to gain business by advertising his particular goods. In similar fashion, the undue proliferation of styles and varieties of goods suggests monopolistic competition rather than pure competition. The fact of the matter seems to be that all of these types of waste exist to some extent at the same time, while none of them are developed to the greatest possible extent.

**Economic Instability** The criticisms of our capitalistic productive system which we have already discussed seem to be valid even when the system is operating very well, but we should also remember that it operates much better at some times than at others. In other words, its operation involves large cyclical swings in economic activity with business booms followed by business depressions, and our major business depressions are extremely serious affairs. From 1929 to 1932, the national income of the United States declined from \$82,691,000,000 to \$40,089,000,000, the number of employed persons decreased from 35,501,000 to 26,195,000, the index number of industrial production (1923-25 = 100) fell from 119 to 64, and the index number of wholesale prices computed by the Bureau of Labor Statistics declined from 95.4 to 64.8. The gross farm income of the country declined from \$12,791,000,000 to \$5,562,000,000, our international trade fell from \$9,640,000,000 to \$2,934,000,000 in terms of merchandise, and the ton-miles of freight carried by our railroads decreased from 450,189,000,000 to 235,309,000,000. The loans and discounts of all active banks fell from \$41,433,100,000 to \$28,089,900,000, the deposits of these banks from \$53,244,700,000 to \$11,126,800,000, securities issued from \$11,592,200,000 to \$1,730,300,000, stock prices from an average of \$311.90 to one of \$80.88 per share, brokers' loans from \$8,549,000,000 to \$244,000,000, and stock sales on the New York Stock Exchange from 1,125,000,000 to 425,000,000 shares.<sup>15</sup> Industrial and commercial failures increased from 22,904 to 31,822, and the number of unemployed increased from a million or so to around 15,000,000.

These breakdowns in the economic activity of our system cause an untold amount of misery and suffering, and most citizens of this country bore some marks of the 1929-32 catastrophe for several years thereafter. Surely no productive system can be considered fully efficient which every few years has to take a protracted vacation during

<sup>15</sup> These data are from the *Statistical Abstract of the United States 1939*.

which it operates at a fraction of its normal rate in the face of unemployed men and resources and a whole host of human wants clamoring for satisfaction. However, business breakdowns or depressions should be emphasized as a distinctive weakness of capitalism only if they seem to be peculiar to this type of economic system.

Unfortunately this seems to be the case, as we noted in Chapter 17. Whichever may be the specific economic factors which should be stressed as generating or cumulative factors in connection with booms and depressions, it seems clear that, from the broad point of view, business cycles result in our system from the combination of modern methods of production and exchange (such as roundabout, specialized, and large-scale production in anticipation of demand) with the institutions of capitalism, including freedom of enterprise, private property, economic motivation, competition, and the money and price system. Modern methods of production and exchange apparently cause no business cycle trouble in the absence of capitalistic institutions (as, for example, in the case of Soviet Russia), and the institutions of capitalism apparently caused very little business cycle trouble until modern methods of production and exchange had developed.

To summarize our previous discussion of the point, roundabout, specialized, and large scale production in anticipation of demand makes for frequent and severe depressions in our economy because our capitalistic institutions make it certain that no one will adjust and coordinate the results produced by various industries and fields of economic activity or plan the final economic results which our system as a whole should produce. Maladjustments of widespread significance must occur in this situation no matter how carefully individuals may plan their own small parts of economic activity. Moreover, since the capitalistic system depends for its operation on the competitive activities of millions of individuals who are seeking to enlarge their incomes and follow their own self-interest, there is a strong tendency for economic activities to be expanded from time to time to an extent which is unsuited to the prevailing distribution of money income. Finally, the combination of capitalistic institutions and methods produces, according to the critics, a fundamental conflict of interests between individuals and society as a whole. While the interests of society as a whole demand not merely a constant but rather a continually expanding volume of productive activity and employment, the interests of private enterprisers, when

faced with the actual or prospective disappearance of "profits," demand from time to time that these enterprisers retrench, curtail production, discharge workers, stop buying materials and supplies, and so on. These activities of business enterprises operate cumulatively to produce depression conditions. Noncapitalistic economies, such as that proposed by socialists, might have a number of economic weaknesses or problems to handle which do not concern us under capitalism, but on this one matter of business cycles it appears that they may have an advantage. That is, as we shall see later, a closely controlled economic system operating on the basis of economic planning should be able to avoid booms and depressions if the planners desire very much to do so.

On the whole, the various weaknesses of capitalistic production should be allowed to qualify to some extent the impression of tremendous efficiency which we gain from the great increases in the volume of production and improvements in methods of production which have occurred in our capitalistic system over the years. While the system has given us both increasing quantities and greater varieties of goods, the improvement in our standards of living has not been nearly so great as it might have been. Moreover, while the standards of living of all levels of the population have improved, the disparity in incomes as between the poor and the rich has not necessarily been lessened.

*The Distribution of Income and Capital Formation.* It is impossible to give wholehearted approval to the arguments in favor of the great inequality in the distribution of income which prevails in our capitalistic system which are based on the effectiveness of this inequality for purposes of saving and capital formation. We may admit, of course, that an economy which aims to be prosperous, efficient, and progressive needs to make use of roundabout, large-scale, and specialized methods of production and that these productive methods require large amounts of capital. We may even admit that most of the saving and capital formation which has actually occurred in our capitalistic system has been due to the activities of persons with large incomes, and that the total volume of savings in our system might well be much smaller than it now is if the national income were equally divided among the citizens and all persons were left perfectly free to save or not to save.

On the other hand, it does not seem very meaningful to say, as some people do, that we should lack something like 90 per cent

of our present volume of production if it were not for the capital supply which has been accumulated over the years One could just as readily say that we should lack 100 per cent of our present volume of production if it were not for the supply of labor at our disposal Since the national income is produced by the cooperation of all the productive agents, it is an unprofitable pastime to try to attribute most of the total to any one productive agent Again, it does not seem to be strictly true that we can have saving and capital formation only by having great inequality in income distribution so that the rich may save large portions of their incomes In the Soviet Russian economy in the last twenty years, saving and capital formation have occurred at a rate which has equalled or excelled any rate which we have achieved in our capitalistic system, and they have occurred without any great inequality existing in the distribution of income among persons Of course, the Russian development has depended upon governmental control of the process of saving and capital formation, and governmental intervention would almost certainly be required to produce an adequate volume of saving and capital formation in our capitalistic system if the national income were rather equally divided While such governmental intervention would be repugnant to many persons, we should remember that our government already intervenes in the process of saving and capital formation upon occasion and that such intervention may be less undesirable than some of the results produced by the great inequality in income distribution on which we now rely for saving and capital formation

It is the notion that we *must* be dependent upon the incomes of the rich for saving and capital formation which is responsible for such statements as "the greater the concentration of income, the greater the gain in national well-being" or "the highest rate of profits will promote the greatest progress and increase of wages" There is no doubt that wages have increased with the growth of capital investment, but it is impossible to prove that these gains in wages would not have occurred if a large part of the national income had not been concentrated in the hands of a relatively small number of persons Moreover, the statement that wages have increased with the growth of capital investment should not be taken to mean that the workers have received all the gains from the growth of capital investment, for it tells us nothing about how the gains have been divided among the various social groups

It does not seem wise to assume blithely that our capitalistic system in practice operates automatically to produce wages for workers which are equal to the workers' contribution to value-product in their respective industries and occupations. In many cases, labor organizations and social legislation may be necessary to insure that workers will receive wages which even approximate the value of their services. And if by chance the workers, under the operation of labor organizations or social legislation, receive as wages a part of the income which would otherwise have been appropriated by the owners of industries, there is no certainty that in the long run the well-being of the workers or of society as a whole will suffer thereby. We cannot even be sure that the volume of saving and capital formation would decline in this situation, and, even if it did, the workers as a whole might gain rather than lose as a result. Any decline in production and wages resulting from a reduced rate of saving and investment might be more than offset by other factors. The workers, since they would receive more adequate incomes, would be relieved of some of the terrible economic insecurity which now operates as a drag on their efficiency and productivity. They would receive enough of the necessities and comforts of life so that they could produce to the limits of their abilities. Those workers who are now, because of certain environmental factors, confined to occupations in which wages are low would in many cases be able to obtain the education and training necessary to permit them to advance to more productive occupations in which wages are higher. On the basis of these considerations, many critics of capitalism hold that the notion that nothing should be done which might interfere with the process of saving and capital formation is simply fetishism. As one writer says:

To put the matter in general terms, there are good grounds for believing that, as things now are, the modern community could achieve a higher standard of productivity and certainly of happiness, if, even at the risk of a substantial decline in the rate of growth of its material (capital) equipment, it devoted more of its resources to improving the quality of its men and women.<sup>16</sup>

If this is true, it seems neither accurate nor fair to say that those who are not satisfied with their lot under capitalism are the incapable, the inefficient, the morons, and the derelicts.

<sup>16</sup> J. Wedgwood, *The Economics of Inheritance* London George Routledge & Sons, Ltd., 1929, pp. 37-38

*Income Distribution and Incentives* In our capitalistic system, most people behave acquisitively in most of their economic activities, and the incentive of economic gain seems to be more powerful than any other incentives in inducing industry, efficiency, and productivity. In this situation, the fact that our capitalistic distribution of income permits extremely large rewards to be received for unusual economic accomplishments undoubtedly furnishes a strong stimulus to many persons. However, it is the opportunity to receive differential economic gains which furnishes the stimulus and not the fact that income is already largely concentrated in the hands of relatively few persons (before taxation). Moreover, it is easy to jump to the dubious conclusion that acquisitiveness is a fundamental and unchanging part of human nature instead of merely a traditional and customary way of behaving under capitalistic auspices. The conclusion that acquisitiveness is inherent in human nature and that any economic system which does not cater to it by providing large differentials in individual incomes is foredoomed to failure cannot be fully accepted until we see how well those economic systems, which rely largely on other types of motivation, can operate in practice.

*The Results of Inequality* It may be well at this point to review the objections which are brought against the inequality which prevails in the distribution of income in our capitalistic system.<sup>17</sup> Such inequality is said to be wasteful at both ends of the distribution. Many families at the lower end of the scale receive such small incomes that they are unable to obtain the commodities and services, and attain the level of economic security, which will permit the workers to function at the full efficiency of which they would otherwise be capable. And the unfortunate results of extremely low incomes are often carried over from one generation to another. At the other end of the income scale there are persons who receive large incomes from property and consume heavily but make no personal contribution to production. Great inequality is also said to be wasteful because it prevents the citizens of the nation from obtaining the greatest possible aggregate of satisfactions from the consumption of a given-sized national income, and because it plays a part, through the over saving of the rich, in bringing on business depressions. We have already noted that there is nothing about a stable degree of inequality in the distribution of income which necessarily predis-

<sup>17</sup> These objections were presented in some detail in Chapter 15.

poses an economy to have business depressions, but, if the degree of inequality increases significantly in a major period of prosperity, this change may play a part in bringing on maladjustment and depression.

These criticisms of inequality suggest that it results in waste and inefficiency, but there are other criticisms which contend that inequality is wrong. One such criticism points to the part which inequality plays in bringing about the misguidance of production and in preventing the adaptation of production to basic human needs and desires, as we noted earlier in the present chapter. Another suggests that inequality in income and wealth is bad because it leads to inequality before the law, in political affairs and relationships with government, in education and culture, in social status, and in business opportunities.

Finally, the great inequality in income distribution which we have is said to be bad because it results to such a large extent from the receipt of unearned income by various persons. Great differentials in income would not be approved even if they were entirely earned and deserved, but the fact that many large incomes contain considerable amounts of unearned income makes them seem still worse from the point of view of the critics of capitalism. By unearned income is meant, for one thing, economic rent. The fact that some individuals or their ancestors have been fortunate or astute enough to appropriate the land which was originally a free gift of nature and are now legally entitled to exact a toll called economic rent from all those who would use their land constitutes no social justification of rent. Since our national land supply would be just as large and of just as good quality as at present even if private individuals were not allowed to own it and charge rent for its use, economic rent as a private income is regarded as socially unnecessary and unearned.

The interest received on inherited capital funds and investments is also often considered unearned. In view of the need of any economic system for an adequate supply of capital, there may be some social justification for the payment of interest to persons who actually save a portion of their money incomes and make capital formation possible, even though not all persons really need an incentive (in the form of interest) in order to save. But there is no excuse to allow persons to reap where they have not sown by receiving interest on capital which someone else has accumulated. However, in de-

sense of this type of income it is often argued that the institution of inheritance would be destroyed for all practical purposes if one's heirs could not derive income from inherited wealth and, since one of the leading incentives to saving and capital formation is alleged to be found in the desire to provide for one's heirs and dependents, the destruction of inheritance would interfere severely with the process of saving and capital formation. This may or may not be true. As a practical matter, it would be very difficult to prove, for many persons without wives or children seem to be just as acquisitive and just as anxious to save and pile up large fortunes as other individuals who have large numbers of heirs and dependents. However, as a practical matter, it would be virtually impossible to arrange things so that interest would continue to be paid on the direct savings of living individuals and would not be paid to individuals whose capital had been inherited, unless we wanted to do away with inheritance altogether. Monopoly profits, nepotic salaries, speculative gains, and income from various types of financial jugglery and chicanery are other types of income which are classified as unearned by many critics of capitalism. All in all, we see that our capitalistic distribution of income is under heavy fire.

*Freedom and Automaticity.* Finally, in considering the alleged weaknesses of our capitalistic system, we must refer again to the questions of freedom and automaticity. Nominally, each individual has a great amount of economic and (usually) political freedom under capitalism. Actually, according to the critics, the poor man is never free. He is not free to seek a better job, to claim the wage he is worth, or to command even a minimum wage for a decent existence. He does not dare to speak his own mind freely, to function as a spokesman for his fellows, or even to join a labor organization in many cases. Poorly educated as he is, the constant pressure of press, radio, theater, and moving pictures leaves him unable even to form an intelligent opinion of the march of events. Legally, he has freedom of enterprise and can become an enterpriser in almost any field of economic activity, but from the economic point of view his chance of becoming an enterpriser is one in a thousand, if not one in several thousand. Legally, he has freedom to select his occupation from among the many which he might fill, but economically, as our system actually operates, he is lucky to have one job, let alone a choice of occupations. Legally, he is entitled to the protection of society in the enjoyment of any amount of wealth and income, however large,

which he may accumulate. Economically, the chances are much against his ever acquiring large amounts of wealth or income. The great captain of industry says "Come," and thousands of people have jobs. He says "Go," and the same thousands are jobless and must depend upon charity or relief for their maintenance. If this be freedom, say the critics, it is the freedom to starve rather than to earn a fair living.

The situation with regard to political freedom is not much better, so it is said. Nominally, there is political equality in our capitalistic system. Actually, the government is firmly, if indirectly, under the control of the rich and powerful, who see to it that the government makes no concessions to the masses which will really jeopardize the position of the powers-that-be. Once in four years or oftener, the great masses of citizens get a chance to elect the holders of public offices, but the opposing candidates are always as nearly alike as Tweedledum and Tweedledee. All that the voters can do really is to decide which representative of the rich and powerful shall hold office during the next term. In the meantime, the captains of industry and finance continue to control the government through their pressure groups, their lobbying and other influence on legislation, their influence on elections, their ability to fight unfavorable laws through the courts, and so on. And at the same time, the captains of industry and finance, through their direct or indirect control of press and radio, manage to convince the common people that they want what they are getting. This picture may be overdrawn by the critics, but it illustrates the difficulty of maintaining political equality in the midst of economic and social inequality.

It is also dangerous to conclude that the capitalistic system as a whole works freely and automatically, independent of control by any individuals or small groups of individuals. We are familiar, of course, with the way in which our capitalistic economy is supposed to operate on the basis of price relationships, but in its actual functioning it is a poor approximation of the ideal theoretical model. Actually, the ownership and control of productive wealth, and hence of productive decisions, are in the hands of a relatively small number of individuals, according to the critics. Corporations now control around two-thirds of the total volume of business in the United States and own almost 80 per cent of all business wealth. Moreover, the ownership of corporate wealth is concentrated in the hands of a small number of large corporations. In 1937, the 394

largest corporations owned about 45 per cent of all corporate wealth, though they amounted to less than 0.1 per cent of the total number of corporations.<sup>18</sup> We had 34 "billion-dollar" corporations in the United States. Each of the two largest of these corporations (the Metropolitan Life Insurance Company and the American Telephone and Telegraph Company) had larger total assets than any of 38 of our states.<sup>19</sup> The number of billion-dollar corporations increased to 43 during World War II. In 1936, the 200 largest non-financial corporations had total assets of over \$75,000,000,000, and the 50 largest financial corporations had total assets of some \$35,000,000,000, a total of \$110,000,000,000 or close to one-third of the national wealth.<sup>20</sup> Corporate income is concentrated in similar fashion. In 1937, 248 corporations received 40 per cent of the total net income of all corporations, though they made up only 0.1 per cent of the total number of corporations with incomes.

It is sometimes argued that this concentration of corporate wealth and income is not very significant, since the large corporations themselves are owned by very large numbers of stockholders. However, in spite of having numerous stockholders, most corporations are controlled by a relatively small number of individuals, and even corporate ownership is not nearly so widespread as is popularly supposed. For example, it has been estimated that one-half of all dividends paid in the United States are received by stockholders who make up less than 1 per cent of all American stockholders.<sup>21</sup> The tendency seems to be in the direction of greater rather than less concentration of corporate wealth and income, for the large corporations seem to get larger since they do the greater part of corporate saving. In 1937, the corporations with assets of \$1,000,000 or more made up only 5 per cent of a group of nonfinancial corporations studied, but they made 88 per cent of the savings of all these corporations.<sup>22</sup>

When we realize that the large corporations of the country are more or less closely interconnected by interlocking directorates and

<sup>18</sup> Temporary National Economic Committee, *Final Statement of Joseph C O'Mahoney*, p. 7

<sup>19</sup> *Ibid.*, p. 5

<sup>20</sup> National Resources Committee, *The Structure of the American Economy* Washington Government Printing Office, 1939, pp. 274-276 and 298

<sup>21</sup> Temporary National Economic Committee *Final Statement of Senator Joseph C O'Mahoney*, p. 8

<sup>22</sup> *Ibid.*, p. 9

interest groups, and that the influential individuals in control of these corporations often play an important part in controlling the government and the public opinion of the country, we can understand why some critics allege that there is a substantial degree of monopoly control over our whole economic system exercised by a relatively small and closely cooperative group of individuals. In such a situation, so it is said, we can hardly expect that consumers' decisions will determine the kinds and quantities of economic goods to be produced, or other important economic matters. The men in charge of our large businesses decide the kinds and quantities of economic goods to be produced and then, by advertising and other forms of cajolery and persuasion, get the consumers to want the goods which are made available for them. The same individuals quite naturally make the most important economic decisions with regard to the volume of saving and investment, the allocation of productive agents among industries and fields of economic activity, and other matters. Thus, our actually operating capitalistic system is said to differ sharply from the ideal theoretical model with its automaticity and flexibility.

**Conclusion** So ends our presentation of the assets and liabilities, or points of strength and weakness, of our capitalistic system. What conclusion should we reach in the end concerning capitalism? This is really a matter for each individual to decide, but there are certain considerations which may be advanced. As everyone knows, our capitalistic system and others like it have been under heavy fire in recent years and especially since 1929. Most of the critics admit that our capitalistic system was a wonderful institution in its day, but assert that it has now outlived its usefulness. A capitalistic system is said to be well adapted to the development and expansion of economic activity in a young country but it is incapable of dealing satisfactorily with conditions in a "mature economy" in which there is no longer any frontier and in which there are no new industries requiring development. This line of argument receives considerable support in times of severe depression, but it is difficult for many people to believe that our economy has reached the ultimate limits of possible growth and that there will be no new industries in the future which will both require development in themselves and stimulate the rest of the economy.

It is also sometimes said that our modern capitalistic system suffers from the "passing of the business enterpriser." With so many

of our industries operated by corporations, business operations have been reduced to routine, and hired managers have taken the place of the old entrepreneurs. In the early days of capitalism, the entrepreneur was really an "enterprising" fellow, who saw visions and dreamt dreams, discovered possibilities of economic development which were unsuspected or unappreciated by the ordinary observers, secured the productive agents necessary for his new undertakings, and gave the enterprises his personal supervision and management, inspired by hopes of direct economic gain. It is held that the ability to perform these functions, though always rare enough, is rapidly disappearing in the modern age. Of course, it may be pointed out that the response which our economy was able to make to the demands of total war in recent years was magnificent and indicated that there may yet be considerable life in the old economic system. On the other hand, it would be answered by the critics of capitalism that our accomplishments of the war period were due in large measure to the temporary abandonment of the traditional capitalistic mode of operation and to the centralization of wide powers for economic planning and production control in the hands of the federal government. While the argument is by no means wholly convincing, it would be held by some people that our wartime experiences really indicated the merits of a planned and controlled rather than a capitalistic type of economic organization.

However, one embarrassing question remains to be answered. If we were convinced that our capitalistic system had become outmoded and needed to be replaced with some other type of system, where should we turn to find a more desirable alternative? The most common answer to this question is, of course, found in the economic system proposed by modern socialists. As we shall see later, the ideal theoretical socialistic economy seems both fairly attractive and rather superior on the whole to actually operating capitalism, but we must not forget that the ideal theoretical system of capitalism would be considered by most people to be superior to actually operating socialism. The question of whether actually operating socialism is superior to actually operating capitalism remains to be answered. Most people would probably be satisfied that the economic experiences of Soviet Russia have not as yet indicated any superiority for actually operating socialism in comparison with our own economy. What the British may accomplish over a long period of years with their system of partial socialism cannot be

foreseen accurately at the present time, but there was relatively little about the operation of this hybrid economy from 1915 to 1948 to suggest that it would make the perfect replacement for capitalism.

If our economic system has a greater per capita productivity with given amounts of productive resources than any other actually operating type of economic system, shall we abandon it because our productive system involves certain wastes and falls short of theoretical standards of perfection? Shall we abandon our economic system because it is subject to business cycles, even if our unfortunate citizens on relief have higher standards of living than many full-time workers in other types of economic systems? Shall we abandon our economic system because of its extreme inequality in the distribution of income, if almost all our workers have standards of living higher than those which the workers enjoy in other systems in which the national income is distributed with greater equality? Where, after all, is the actually operating economic system which produces more desirable economic results, on the whole, than our own? Arguments of this sort may not be wholly logical, but there can be no doubt that many of us will be convinced by them and will fall back on the old proposition that "seeing is believing." That is until we can see other economic systems operating in a fashion which indicates clearly their economic superiority in comparison with our capitalistic system, most Americans will probably be content to get along with what they have.

#### QUESTIONS

- 1 "The task of evaluating any economic system as a whole is extremely difficult and complicated." Explain.
- 2 "Our capitalistic economy, operating on the basis of the price mechanism, does a well-nigh perfect job of adapting production to basic human needs and desires." Show whether you agree.
- 3 "Once decisions have been reached as to what commodities and services should be produced our capitalistic economy proceeds to produce these goods with great efficiency." Do you agree? Explain.
- 4 "The supporters of capitalism produce several arguments in favor of the great inequality in the distribution of income which characterizes our system." Explain.
- 5 "Our capitalistic economy furnishes a large measure of political and economic freedom for the individual citizens." Show whether you agree.

- 6 "Our capitalistic system is desirable because it works freely and automatically" Discuss
- 7 Why do supporters of our capitalistic system argue that business cycles are not inherent in the nature of that system? Explain
- 8 "While admitting its accomplishments in the field of production, critics of our capitalistic system contend that it is not nearly so productive as it should be" Explain
- 9 "The critics hold that our capitalistic system does a very poor job of adapting production to basic human needs and desires" Why?
- 10 "The efficiency of our capitalistic productive system is not nearly so great as it should be" Give at least three good arguments in support of this proposition
- 11 What do critics mean when they refer to the abuse of the profit motive in our capitalistic system?
- 12 Describe the so called competitive wastes of our capitalistic system
- 13 A socialist says "In the capitalistic system of the United States, entrepreneurs abuse the profit motive and indulge in many types of competitive wastes Both of these developments are increasing in magnitude as time goes on" Criticize this statement
- 14 Should great inequality in the distribution of income under capitalism be approved on the ground that such inequality is favorable to saving and capital formation? Explain
- 15 Summarize the objections which are brought against the great inequality which prevails in the distribution of income in our capitalistic system
- 16 Why do critics of our capitalistic system argue that most individuals enjoy very little economic and political freedom in that system?
- 17 "The conclusion that our capitalistic system operates freely and automatically, independent of control by any individuals or small groups of individuals, is at least partly unsound" Show whether you agree
- 18 What conclusion do you reach in the end concerning the desirability of our capitalistic system? Explain

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## CHAPTER 23

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### **EVALUATION OF SOCIALISM**

IN considering the desirability or undesirability of the economic system proposed by modern socialists, it is not entirely satisfactory merely to evaluate the socialistic economy as a going concern. For many persons, the answer to the question of whether socialism is desirable would depend upon the methods by which it is proposed that we pass from capitalism to socialism as well as upon what a socialistic economy would be like after we had reached it.

#### *The Transition from Capitalism to Socialism*

***The Dangers of Revolution*** The issue of revolution *versus* evolution is an important one in connection with the transition from capitalism to socialism. There are some socialists, though they are probably in the minority in the United States, who think that socialism can be achieved only by revolution, or violent overthrow of the existing capitalistic system. These socialists are not necessarily any more bloodthirsty than the others, but they apparently feel that there is no real chance for a peaceful, orderly, evolutionary transition, because the capitalist class is strong and well defended and there seems to be no satisfactory agency available for molding public opinion so that the citizens will want socialism and will vote it into power.

On the other hand, there is no doubt that revolution (in the sense of violent overthrow of the existing system) is a dangerous and unsatisfactory method of transition. It would be likely to involve much destruction of wealth and loss of life. Under these conditions, and especially if many of our leading managers and enterprises were "liquidated," the new socialist economy would be off to a poor start and would be considerably handicapped. It may be that much managerial talent is now going to waste in the ranks of the workers.

because of lack of opportunity, but such talent would have to be trained. It would not be possible to put an ordinary worker in charge of a modern productive establishment and expect it to function efficiently. In the second place, if the revolution were not quick and decisive, it might produce a rather complete breakdown or stoppage of our productive and distributive processes. The cost of such chaotic conditions in terms of human life and suffering cannot even be imagined, but it is safe to say that the economy would bear the marks of revolution for years if not decades to come.

If a revolution is attempted but does not succeed, the result is likely to be a tremendous swing in the direction of conservatism, reaction, and repression which will make further attempts impossible for a long time. On the other hand, the methods of peaceful persuasion which are intended to induce the citizens to vote socialism into existence, if they fail in a given instance, can be tried over and over again until ultimately success may be achieved. There is the further question of whether a successful revolution is at all possible at the present time. Many years ago, a revolutionary group had some chance to be about as well armed as the defenders of the existing system, but at present the tanks, airplanes, and other weapons of the armed forces of the nation can scarcely be duplicated by the revolutionary elements. A successful revolution seems hardly possible unless the armed forces of the country go over to the side of the revolutionists. After a successful revolution, it is usually necessary for the government to be a strong dictatorship in order to suppress opposition elements and guard against the threat of counter-revolution. However, it is ordinarily much easier to set up a dictatorship than to get rid of one, and the dictatorship may go on indefinitely, preventing effectively the establishment of that economic and political democracy for which modern socialists hope. In any event, starting a revolution to obtain socialism is like paying 25 cents to draw a parcel out of the "grab-bag" at a church fair. A revolution may be aimed at achieving socialism, but the country may find itself saddled with fascism after the smoke of battle has cleared away. Finally, the knowledge that socialists aim to teach their system by means of revolutionary tactics may alienate in advance many intellectuals and middle class people who would favor socialism as a matter of general principle or at least would not be greatly opposed to it.

*The Prospects of Evolutionary Transition.* For all these reasons, most socialists in the United States do not favor violent revolution as a means of transition from capitalism to socialism. But, a peaceful and orderly change to socialism presumably involves convincing enough people that they want socialism so that they will vote it into being and it is not clear just what available agency would be adequate for this task. Newspapers, radio, and other agencies for influencing public opinion are, of course, useless for this purpose since in the main they are owned or controlled by individuals whose interests demand the perpetuation of the existing capitalistic order. One could also scarcely imagine the citizens of the country, since they are not generally indoctrinated with socialism, permitting the schools to be used to advance the principles of socialism. Labor unions constitute a possible vehicle for this purpose, and some investigators seem to be convinced that many of our labor organizations are already hotbeds of socialism or worse. However, it is our conviction, contrary to the findings of certain investigating committees, that most American labor organizations are as capitalistically minded as the capitalists themselves, and that they are bent on obtaining economic gains within the existing capitalistic system rather than on changing that system to something else. We have, of course, a busily working Socialist Party in the United States, but thus far it has seemed completely incapable of convincing any large number of citizens that modern socialism is a system greatly to be desired. On the whole, the problem seems to be most formidable.

*The Confiscation of Productive Wealth.* If we assumed that it had been decided that the change from capitalism to socialism should be made, the next issue would concern the method by which productive wealth (land and capital) should be transferred from private to public hands, for this transfer is fundamental to the operation of socialism. In other words, should we confiscate this productive wealth, pay the present owners for it in full, or give them partial compensation? It is to be supposed that many socialists would favor outright confiscation as a matter of principle, but as a practical policy confiscation leaves something to be desired. In the first place, it would almost necessarily involve sudden if not revolutionary socialization. A gradual process of confiscation would be virtually impossible. There would seem to be no very good reason why the productive wealth of some individuals should be confiscated at once while that of other individuals should be left un-

touched for a time. Moreover, the beginning of the confiscatory process would bring to a halt all new investments in industries still in private hands and would probably cause the present owners of these industries to fail even to maintain and repair their present productive facilities. With confiscation soon to come to all industries, the values of productive wealth still in private hands would fall to very low levels, if not to zero. Confiscation would violate the ethical standards of many of our citizens, in the sense that it "just would not seem right" to deprive people of their wealth without any compensation, and some supporters of socialism might be alienated. Finally, to the extent that the productive wealth of this country is owned abroad, confiscation might lead to various international complications.

*Full Compensation for Productive Wealth.* Full compensation for the present owners of land and capital might involve condemnation proceedings, with the value of the productive wealth to be determined later, but a more likely procedure would be for the government (representing society as a whole) to buy out the present owners, give them government bonds for their land and capital, and pay interest and principal out of the earnings of industry. Full compensation in cash would amount to confiscation. Since further private investment in productive wealth would be impossible, cash compensation payments amounting to hundreds of billions of dollars in paper money would have very little purchasing power or value. In any case, full compensation for the present owners of productive wealth would be repugnant to the supporters of socialism. If bonds were issued to the full value of the land and capital, the present owners would probably not regard themselves as fully compensated unless these bonds could be transferred from person to person and could be passed on to the heirs of the present owners. Thus, full compensation would lead to the continuation of several practices which the socialists consider objectionable in our present capitalistic order. The present owners would be assured of perpetual incomes and many of them could continue to live well without needing to work even under socialism; trade and speculation in securities would still be with us, and the evils of inheritance would continue.

*Partial Compensation for Productive Wealth.* Therefore, the most practical policy from all points of view would seem to be one of

partial compensation for the present owners of productive wealth In this process, it might seem desirable to discriminate to some extent between different classes of owners and different classes of productive wealth Much less compensation might be given to owners of land or inherited wealth than to persons whose capital is the result of their own savings Owners of small amounts of productive wealth might be compensated more fully than owners of large quantities of productive wealth Owners who were young, intelligent, and well trained so that they could probably make a good living for themselves in the new socialistic order might be given relatively little compensation for their wealth, while owners who, because of old age or lack of ability, could be expected to accomplish very little in the future might be treated much better

In any case, government bonds would probably be given to the present owners of land and capital up to the full value of their wealth, probably on the basis of its last recorded value under capitalism The compensation would then be made only partial by paying low rates of interest on these bonds Any necessary or desirable discrimination could be practiced by varying the low rate of interest to some extent from one class of bond receivers to another The bonds would be nontransferable, so that they could not be traded in or inherited, and they would be dateless, so that the principal sum involved would never have to be paid off All that they would involve, therefore, would be the right to receive a certain income for life In the case of old people, who would find an income for the rest of their lives rather unacceptable, the government might guarantee a certain fixed number of annual payments either to these people or their heirs In all cases, however, the annual payments of income on these bonds would cease after a limited number of years The bonds would be unsecured by any lien on the productive wealth transferred to the government and would carry no rights of control even if the expected income were not received in a particular period Such a method of compensation would probably not seem highly desirable to many present owners of land and capital, but it would be better than outright confiscation

In a larger sense, of course, it is impossible to transfer productive wealth from private to public hands without confiscation If the present owners of land and capital are given nothing, the confisca-

tion is obvious, but, if they are to be compensated in full, this means that the government must confiscate a large part of the incomes of all the citizens through taxation in order to pay interest and principal to the present owners of productive wealth. If the burden of the taxes is placed entirely on the persons who are to receive interest and principal, there is once more outright confiscation in reality. Finally, under a system of partial compensation, the burden of confiscation will fall in part on the present owners of land and capital and in part on the other citizens who must pay taxes in order that the present owners may receive the annual incomes which represent their partial compensation.

*The "Flight of Capital."* In all this discussion, we have paid no attention to what some people consider a leading problem in this field. That is, they contend that the coming of socialism, or even the serious threat of its coming, would cause large quantities of capital to flee the country. Since it is physically impossible for most factories, machines, and industrial locations to get up and flee, this contention must mean that productive wealth would be converted into cash which would be transferred to other countries. However, even if productive wealth could be converted into cash, the problem of transferring its value out of the country would be insuperable. Such a large additional demand for foreign exchange would quickly drive rates of exchange to the gold-exporting point, if gold exports were permitted, and our large gold supply would be inadequate for transferring the value of all productive wealth out of the country even if it could be used for this purpose. If gold could not be used, the great demand for foreign exchange would drive rates of exchange so high that only very small amounts of foreign purchasing power could be obtained for large amounts of our domestic purchasing power. In any case, before the problem of transfer could arise, how would the present owners of land and capital convert their holdings into cash? The only method would be to sell the productive wealth to someone, and we may well wonder who would buy it and how much they would pay for it if it were known that the productive wealth would soon pass into public hands. On the whole, then, there seems to be no reason for thinking that the advent of socialism could deprive us of any large part of our productive wealth or that the present owners could escape with much of the value of their holdings.

*The Probable Accomplishments of  
Modern Socialism*

**The Methods of Production** We must now turn from the problems involved in passing from capitalism to modern socialism to a consideration of the results which a system of modern socialism might accomplish, if such a system could be reached. In the general field of productive activity, our discussion in previous chapters has indicated that there would be many similarities between modern socialism and capitalism. Most economic principles in this field are valid for either type of economic system, and a socialistic economy would make use of the methods of roundabout, specialized, and large-scale production in anticipation of demand. Many types of establishment organization and of combinations of productive establishments might be used under socialism as under capitalism. Money and prices would be used under socialism, both commercial and investment credit would be necessary, and banks would exist undoubtedly to dispense these types of credit, though the banks would be socially owned and operated, and the total amount of each type of credit to be extended would be subject to planning. The process of saving and investment would involve the same fundamental costs and produce the same basic physical results in both systems. The business of getting finished goods into the hands of the final consumers would be handled under socialism by stores which would closely resemble those of a capitalistic system as to type and methods of operation. The physical rationing of goods to consumers is no more indispensable to one system than to the other. Finally, there is no need for any profound difference between modern socialism and capitalism with respect to international trade and commercial policies.

In the field of production, as elsewhere, the fundamental differences between modern socialism and capitalism have to do with institutions. Under socialism there would be no private property in productive wealth (for all practical purposes), little if any freedom of enterprise in the ordinary sense, and a sharply reduced dependence on the economic motivation of the individual citizens. All this means that, under modern socialism, all the major industries and fields of business activity will be almost entirely government owned and operated, and that most of the important types of economic

decisions will be made by public authority on the basis of economic planning rather than by private individuals on the basis of the market and price mechanism. In the field of production, then, the controversy over the merits of socialism settles down to two issues. First, would the total results of planned production be better suited, on the whole, to the basic needs and desires of the people than those achieved by capitalistic production on the basis of the market and price mechanism? Secondly, is there any reason for assuming that planned control over production (using the same principles and methods in the actual carrying on of production) would be able to achieve greater technical efficiency in production than that attained under capitalism?

*Adapting Production to Human Needs and Desires.* With regard to the first of these matters, two rather significant advantages may be claimed for socialism. In the first place, it may be claimed that a socialistic system, in planning for production on the basis of human needs, would have an advantage over capitalistic systems, in that it would not produce the "wrong kinds of goods." This means, in part, that certain commodities which are considered, by rather common consent, to be noxious or harmful to the users would not be included in socialistic plans for production, even though large numbers of misguided individuals could be persuaded to purchase these commodities in the market at prices that would cover or more than cover their costs of production. It would also mean that the socialist planners would consider the full social costs of producing various types of economic goods and not merely those costs which under capitalism are reflected directly in the prices of productive agents in the market.

Somewhat more important is the fact that a socialistic economy, in planning for production on the basis of human needs and desires, almost certainly would not produce trivialities and super-luxuries for some of the citizens while other individuals were inadequately supplied with the common necessities and basic comforts of life. Limousines, yachts, and palatial homes would not be produced for anyone until all consumers were assured of adequate food, clothing, shelter, and other economic goods. To be sure, a socialistic economy would have differences in money incomes between individuals, and these differentials might be moderately large, but we must remember that the kinds and quantities of goods to be produced under socialism would be controlled by economic planning and not by the

money prices which individuals were willing to pay for various goods in relation to the money costs of producing them. That is, individuals with fairly large money incomes would not be allowed to use them to divert productive resources to the satisfaction of their relatively less important wants unless and until the basic wants of all the people had been rather well satisfied.

In the second place, a socialistic economy should have an advantage over a capitalistic system in providing for the non-market wants of the people, such as the desires for full employment, complete social security, a high level of public health, and other things. In a capitalistic system, transfers of income from the private sector of the economy to the government probably must be held within certain limits if the system is to be able to continue to operate in capitalistic fashion, and there is some question anyhow as to whether the government could guarantee full employment or complete social security without assuming a large measure of responsibility for the operation of the whole economy. Under socialism, with the government owning and operating most industries and businesses, all conflicts between "government" and "business," financial or otherwise, would tend to be eliminated. Presumably the government of a socialistic system could devote any share it pleased of the national income to the performance of social services, subject only to the limitation that devoting more of a given-sized national income to these purposes would leave less for other purposes.

*The Problem of Technical Efficiency* In considering the probable technical efficiency of enterprises and industries under socialism, we cannot accept the popular capitalistic opinion to the effect that a given enterprise or industry, when operated by the government, must always run less efficiently than it would in private hands. Nor can we rely on the success or lack of success experienced by the government of our capitalistic system in operating the railroads or some other private industry in wartime. When the government operates a single industry under conditions of great emergency and with other major industries still in private hands, the situation simply is not that of modern socialism.

In dealing with the general situation, we may realize that private enterprises may have the advantage over governmental enterprises in businesses in which continuous invention, flexibility, and adaptation to changing conditions are important. That is, private enterprises are likely to have greater freedom of action, greater readiness

to try new methods or new products, greater willingness or ability to take risks, and a greater drive to achieve efficiency because of the possibility of profits. On the other hand, there may not be so much to choose in this respect as between great capitalistic corporations and large governmental enterprises, for the managers of large corporations are often rather thoroughly tied down by their obligations to boards of directors, corporation laws, auditors' requirements, technical methods laid down by experts, and arrangements with other companies.

It is sometimes held that private enterprises under capitalism are more likely to reach the optimum size for efficiency than are governmental enterprises under socialism, for the competitive struggle under capitalism is supposed to eliminate firms which are too large or too small. However, the firms in many capitalistic industries are not genuinely independent and competing, and in such cases the problem of attaining optimum size of firms is not very different from that which the economic planners would face under socialism. Another advantage of capitalism from the point of view of technical efficiency is supposed to be found in the fact that inefficient firms fail and go out of business in that system, while socialistic enterprises would continue to operate even though they were inefficient. However, this advantage for capitalism would be realized only under strictly competitive conditions. When capitalistic industries are controlled by two or three large firms, these firms may not be under great pressure to operate with utmost efficiency lest they be forced out of business, and, in any case, failure is likely to mean only a financial reorganization rather than the cessation of production. Finally, we must note that some capitalistic industries are already subject to governmental regulation. Such industries are no longer free to realize to the full the advantages of strictly private businesses, and the costs of necessary regulation should be taken into consideration in reaching decisions as to the efficiency of these industries under capitalism.

Apart from these considerations, some definite advantages can be claimed for socialistic production in connection with the question of efficiency. In a capitalistic system, conflicts between government and business affect not only the kinds of things which the economy can set out to produce for the people, as noted above, but also the efficiency with which business enterprises can operate. Under socialism, with the economic life of the country no longer divided into

public and private spheres, much friction, hostility, and litigation could be avoided Moreover, some problems of public finance might be eliminated, since it would not be necessary for the socialistic government to pay out to the citizens more money income than would be required for purposes of private consumption and then proceed to recover a part of it through taxation

It is claimed as an advantage of socialism that production would be for use rather than for profit Technological advances and innovations of all kinds would be freely available and could be used by all firms that had need of them, and socialistic production would involve no restriction of output or abuse of the profit motive, since private individuals would not control production and there would be no one to gain from a policy of restrictionism All major industries would be owned and operated by society as a whole, and it is perfectly obvious that society as a whole cannot gain by restricting production The general restriction of production can mean only poverty for a whole society Moreover, since the real commodities and services at the disposal of consumers under socialism cannot be increased or decreased one whit by the fact that the economy as a whole operates at a money profit or a money loss, a whole society can be tremendously indifferent to the making of money profits Prosperity for a society as a whole is to be found not in profits but in plenty The advantage of production for use is considered extremely important by the supporters of socialism

Since planned production would not be dependent upon the competitive activities of large numbers of private persons, it is thought that most of the "competitive" wastes of capitalism could be eliminated under modern socialism In deciding how much of a particular economic good to produce, the economic planners might or might not reach a decision which was well suited to basic human wants, but, after deciding upon the output to be produced, they should at least be able to avoid the folly of setting up enough productive facilities to produce double that output and then allowing half of these productive facilities to stand idle On the other hand, the planners might provide for some productive capacity to be temporarily unused to allow for prospective population growth or expansion in demand One could not imagine, however, that the Socialist Petroleum Company of America would erect gasoline filling stations on all four corners of busy street or road intersections to sell different brands of essentially the same gasoline to the consumers, or

that the local socialist milk company would send a dozen wagons or trucks through each city block to sell different brands of essentially the same dairy products to the consumers, with each vehicle serving only here and there a household.

Although the individual consumers under socialism would undoubtedly desire a bit of variety in their consumption and the economic planners would be willing to make some concessions to this desire, it is hardly likely that the planners would see fit to undertake the production of almost a million varieties of axes or almost 13,000 varieties of solid section steel windows. Again, it is most improbable that the economic planners, in arranging for the production of any given commodity (such as cigarettes, for example), would decide to turn out dozens of closely similar brands and then devote fabulous quantities of productive agents to the production of advertising designed to induce the citizens to consume each of these various brands in preference to all the others. Educational and informative advertising might have some place even in a socialistic economy, but competitive or combative advertising just would not make sense from the point of view of society as a whole.

It is also difficult to believe that the governmental enterprises of a socialistic system, in exploiting the natural resources of the country, would have any incentive to mine coal in such a wasteful fashion that large parts of the natural deposits would be left in the ground in such a condition that it would be practically impossible to remove them later on, or to drill oil wells in such great numbers in a given field as to interfere seriously with the removal of this resource from the ground. Since the waste in the exploitation of natural resources under capitalism is attributed largely to the competitive organization of the industries in question, the elimination of competition should go far toward the elimination of the waste.

Having thus disposed of the competitive wastes, we note finally that one of the most important probable accomplishments of a socialistic economy in connection with efficiency in production would be found in the achievement of economic stability. In other words, such an economy should be able to avoid business depressions and unemployment if the citizens and the economic planners greatly desired to do so. We have noted as one of the weaknesses of our capitalistic economy the fact that, while careful economic planning goes on in individual enterprises and industries, there is no one to plan the economic results which the system as a whole should ac-

complish or to perform the difficult task of adjusting and coordinating the operations of the various industries and businesses of the system. Under socialism, on the other hand, the aggregate results desired from economic activity would be planned before the individual phases of this activity were undertaken. If the economic plans were well made and well carried out, the total economic results produced should be more steadily in accord with basic social needs and desires than under capitalism and there should be a striking absence of those serious maladjustments between industries and fields of economic activity that are so important a factor in producing business depressions and unemployment under capitalism. Moreover, with industries in the control of society as a whole, there would be no competitive enterprises to overshoot the mark and produce industrial over-capacity with respect to effective demand on the market.

All this does not mean that no mistakes will be made in economic planning nor that the plans which are made will be perfectly carried out. The planning commission may decide that the shoe industry should turn out 150,000,000 pairs of shoes next year and sell them at an average price of \$5.00 a pair. When the next year rolls around, the output of the industry may come up to the planned estimate, but it may be found that the consumers of the system will purchase this quantity of shoes only if the prices average \$8.00 per pair. This looks like a familiar capitalistic type of maladjustment, but the point is that under socialism this mistake will not cause the shoe industry to go into a tailspin nor cause its productive facilities and workers to stand idle for a time. In all probability, the prices of the shoes would be reduced to such an average level that the entire output of the industry would be taken off the market, and the industry would go merrily about its business of producing shoes. But, it may be objected, in that case would not the shoe industry's receipts from sales fail to cover its costs of production? One answer to this question is, of course, that the relationship between money prices and costs would not be highly significant in a socialistic economy. However, if there were any desire to cater to those who are particular about having prices cover costs, all the economic planners would have to do would be to revalue in a downward direction the productive facilities devoted to shoe production, and then even the reduced prices of shoes would once more cover their costs. With both prices and costs subject to the arbitrary control of the economic planners,

under socialism, they could always be made to balance each other, if desired, and in the meantime economic activity would go on and on.

Or suppose, as would often happen, that the outputs of various industries did not reach the amounts that had been planned. If cattle and hog production lagged behind planned estimates, it would be impossible for meat-packing establishments to use their productive facilities and workers at the planned rate. The production of automobiles, machines, and other steel products could not be long maintained at the planned level if the production of iron ore and coal fell far short of planned estimates. Once again, however, the point is that under socialism these maladjustments would not necessarily leave large numbers of workers with nothing to do except to stand idle and contribute, through their loss of income, to conditions of depression and unemployment for other industries and groups of workers. Since society as a whole, as the only real enterpriser under socialism, does not have to make profits from the employment of workers, it would never be too difficult to find commodities for all the workers to produce. Workers or other productive agents are "profitably" employed from the social point of view so long as they produce commodities or services which the members of society need or desire, a concept which furnishes virtually limitless possibilities for employment in view of what is known about the nature of human wants.

A socialistic economy would be in a good position to handle another matter which, according to some business cycle theorists, is of considerable importance in connection with business cycles under capitalism—the relationship between saving and investment. At times under capitalism, the volume of saving exceeds that of investment, and savings pile up in the banks, unable to find takers, while at other times the volume of investment exceeds that of the current savings which are voluntarily made. Such conditions tend to cause business depressions in the one case and business booms in the other. Under socialism, since the economic planners would be in control of both processes, it should be possible always to keep saving and investment in balance. All productive agents which were withheld from contributing to the immediate satisfactions of consumers would be used for the production of capital goods, and all sacrifices of consumers in going without consumers' goods at present should bear fruit in the form of new capital goods which would

enhance future productivity. The amount of saving and investment decided upon by the planners might or might not be in accord with the immediate wishes of the consumers, but the planners would not be so foolish as to keep productive agents from producing goods for the immediate satisfaction of consumer wants and at the same time fail to use these productive resources to turn out new capital goods.

The basic point in all this discussion is that the conflict of individual and social interests which exists under capitalism would be resolved under socialism by taking the control of production and of economic activity in general out of the hands of private individuals and placing it in the hands of society as a whole. Business depictions could be avoided under socialism, so it is said, because there never would come a time in the expansion of productive and distributive activities when, because of considerations of money profit and loss, it would be necessary or desirable for society, as the only enterpriser of importance, to retrench, cut production, discharge workers, and curtail the purchases of materials and supplies. With productive and distributive activities adapted to social needs, there would be virtually no fear of business cycles, because there are no cyclical fluctuations in social needs for economic goods which would produce other cyclical fluctuations in economic activities.

*The Distribution of Income.* We have already seen that the production of the "wrong kinds of goods"—a problem which is associated with great inequality in the distribution of income among persons and families under capitalism—would be eliminated by planned production under socialism. The other evils which result from great inequality under capitalism would also be eliminated or greatly reduced under the sharply lessened inequality in the distribution of the national income to which modern socialism aspires. Moreover, the remaining inequality in the distribution of income would be approved by the people since it would result almost entirely from differences in wages and since rent, interest, profits, and other condemned or questionable types of income would be eliminated as distinctive private incomes received by some persons but not by others. As we have seen in our longer discussions of income distribution, a socialistic economy could scarcely eliminate all the basic economic causes of rent, interest, and profits, and these types of income would continue to exist as portions or sections of the national income. But the national income from all sources, or such part of it as was available for consumption, would be distributed to

the citizens in the form of wages, and all citizens would share in any rent, interest, and profits produced by the system so that these sources of income would not prove to be of special advantage to any individual citizens or groups of citizens.

Because of the relatively equal distribution of income under socialism, the great masses of workers (unskilled, semi-skilled, and skilled) would be relatively well off in comparison with their status under capitalism. According to the prospectus of modern socialism, differences in wages as between occupations and groups of workers would still be based upon differences in the marginal productivity of the workers, and yet the differences would be relatively small. This result would be produced for the most part by two factors. In the first place, widespread opportunities for receiving education and training would help to break down the purely environmental barriers between the so called noncompeting groups of labor and would permit each worker to get into the most productive and highest paying occupation for which his native abilities permitted him to qualify. This would mean that the unskilled and semi-skilled groups of labor would not be nearly so overcrowded as under capitalism, while larger numbers of workers should find their way into skilled occupations, managerial positions, and the professions. This partial equalization of the numbers of workers available in the various groups should go far toward reducing differences in the marginal productivity of labor from group to group. In the second place, the marginal productivity of the various workers and groups of workers under socialism would be determined by a process of social evaluation (by the economic planners) and not by the values of their products as determined in a free market. However great the efficiency of the most highly skilled managers of enterprises or industries or the talent and ability of leading doctors, lawyers, or actors might be, it is doubtful that the economic planners would ever consider their services to be worth several thousand times as much per year as the services of ordinary workers—and yet relationships of this kind actually exist in our capitalistic system. Apparently, then, the great majority of our workers would be better off with respect to wages under socialism than they are at present, if only the total amount of the national income to be distributed remained as large as it is under capitalism.

Quite apart from the question of money wages, the status of labor under socialism would be desirable in other respects, according to

modern socialists A socialistic economy would be able to provide employment for all the workers, and relief from the bogey of unemployment would be a great boon for labor Social insurance covering accidents, illness, old age, death, and other risks would be provided, and the size of the benefits, as well as other characteristics of this insurance, would probably be more satisfactory than under capitalism In a socialistic economy, an increased amount of attention would be given to preventive medicine, free medical services and adequate hospital facilities could be provided for all, and enlarged opportunities to study medicine and engage in medical research would be furnished to the citizens Fairly large quantities of resources would be devoted probably to the furnishing of educational services, recreational facilities, parks, playgrounds, theatrical performances, concerts, and possibly low-cost travel Finally, workers could have their labor unions very much as at present, and these organizations would still have a number of useful functions to perform

*The Issue of Freedom* Finally, according to the socialists, all the economic accomplishments which we have described would be consistent with the retention of a great degree of political and economic freedom for the individual citizens The government of the socialistic system would be democratic in form and substance, it would make immediate and precise responses to the changing desires of the citizens, and the will of the citizens would be enlightened by means of education and the furnishing of opportunities to hear and understand all sides of the various issues on which the government had to pass Economic representation in legislative bodies would strengthen the ties between economic activities and government While operation of the economy on the basis of economic planning would necessitate the placing of great economic powers in the hands of a very small group of people at the head of the system, the planners would be ultimately responsible to the citizens That is, if the planners did not produce results in accordance with the basic desires of the people, the indignant citizens could and would turn the planners out of office at the next election

In addition to having ultimate control over the economic decisions and activities of government, the individual citizens under socialism would have considerable economic freedom in their own right To be sure, the institutions of freedom of enterprise and of private property in productive wealth would not exist, for all prac-

tical purposes, but socialists contend that the existence of these institutions means very little to most individuals under capitalism. The individual would have no chance to start life as a poor boy and end it as an extremely rich old man, but many more individuals than under capitalism would have a real opportunity to rise from lowly to at least moderate circumstances. To make up for the loss of freedom of enterprise, the individual would have a free choice of occupations under socialism, and the breaking down of environmental barriers to movement between occupations in different labor groups would make this free choice of occupations an economic as well as a legal reality. Moreover, the individuals of the system as consumers would have freedom of choice and could spend their money incomes for any desired assortment of the commodities and services which the economy produced.

### *The Probable Failures and Weaknesses of Modern Socialism*

*Problems of Planned Production* In considering the probable failures and weaknesses of a socialistic economy, we turn once more to the question of production on the basis of economic planning. Since, as we have seen, the productive system under socialism would make use of many productive methods and principles which are also employed in our capitalistic system, the fundamental issue in production concerns the probable effectiveness of planned control over production as compared with control by the market and price mechanism. In this connection, we are concerned with two questions—the extent to which the planned productive results, if these results could be attained actually, would be suited to the basic needs and desires of the citizens, and the extent to which the socialistic economy would probably achieve efficiency in pursuing the planned productive results. On the first of these points we cannot blithely accept the common socialistic opinion that planned productive results could scarcely be worse than those of unplanned capitalistic production. It is true, as we have seen, that planned production would have some advantages in comparison with capitalistic production, but these advantages certainly do not mean that the planned productive results will necessarily be perfectly suited to the fundamental needs and desires of the people, for planned production has some difficulties which are distinctly its own.

Under socialism, many important economic decisions, such as those concerning the kinds and quantities of goods to be produced, the allocation of available productive factors to various industries and enterprises, and the distribution of productive resources between providing for present consumption and providing for capital formation, must be made by the economic planners. And the planners cannot rely on the customary capitalistic guides of prices and costs in making these decisions, for prices and costs are not determined in the market under socialism but are in the power of the same planners who might otherwise wish to rely on them for guidance. Under these conditions, it is usually held that the important economic decisions would be made "arbitrarily" rather than "rationally." Of course, the decisions of the planners would be "rational" in the broad sense of that term, but they would be "arbitrary" in the sense that they could not be made on the basis of prices and costs as independent data.

However, it is sometimes held that rational decision-making would not be impossible under socialism if it were possible to simulate the results of the capitalistic pricing system without actually having that system. Many writers have developed complicated theoretical processes for achieving this result, and we examined some of these plans in detail in Chapter 5. Without going over this material again, we may refer to our former conclusion that it would be possible, at least in strict theory, for a socialistic economy to achieve something approaching rational decision-making on the basis of one of these artificial procedures, but the procedures are so complicated that it is doubtful that any economic planning agency would attempt to follow any of them in practice. It is probable that the economic planners under socialism would decide to make the basic economic decisions on their own power.

In trying to determine what the people wanted, and hence the kinds and quantities of goods which should be produced, the economic planners could get some help, of course, from their knowledge of what people in general have consumed in the past, and could make adjustments on the basis of what people in good, though not rich, circumstances have consumed under capitalism. Further guidance could perhaps be obtained by appealing directly to consumers to specify what they wanted, and by making use of the opinions of experts or of advisory bodies of consumers. The planners could also have a certain quantity of a good produced and offered

for sale at a certain price and could observe the eagerness or reluctance with which consumers purchased the good. But this would not tell the planners much, since the demand for a particular good at a particular price when other goods were not available or were available only in small quantities at high prices would be quite different from the demand for it when other goods were available in large quantities at low prices.

In spite of all the devices which might be used in trying to ascertain the desires of the citizens, there would remain quite an element of arbitrariness in the decisions of the economic planners, and they could never be certain as to the quality of their decisions. They would know, of course, that a large amount of a good is usually to be preferred to a small amount, but, having decided to produce a given quantity of a good through the use of given quantities of the productive agents, they would never know whether that quantity of that good would give more satisfaction than would the quantity of some other good which could have been produced with the same quantities of the agents of production. And, of course, if planned decisions as to the kinds and quantities of economic goods to be produced left something to be desired, the same thing would be true of the allocation of productive agents to industries and businesses on the basis of these decisions.

In similar fashion, decisions of the planners with regard to saving and capital formation *versus* present consumption would always be suspect. If the planners were faced with the choice of two methods of producing a certain good and if one method would produce a relatively small amount of it almost at once, while the other method, since it required the prior construction of large quantities of capital goods, would produce a much larger amount after a considerable elapse of time, the planners would be unable to make a completely rational choice between these alternatives in the absence of a market-determined rate of interest. The planners would certainly be expected to take the time factor into consideration, but again they could never be sure of the quality of their decision. They could observe whether the citizens as consumers registered satisfaction or dissatisfaction over the planned decisions with respect to saving and capital formation, and the resulting limitations on immediately available consumers' goods, but the planners could never be sure just how good or bad their decisions had been on the basis of the time preferences of the individual citizens.

These considerations seem to indicate that, even in the absence of certain capitalistic shortcomings in the field of production, there would be ample opportunity for the total results of planned production to fall short of perfection in the matter of adaptation to human needs and desires. And this is not the whole of the story for we have thus far been assuming that the planners are men of good will who struggle manfully to fulfill the desires of the people. If the planners were proud in their wisdom and decided that they knew what the people wanted better than the people themselves knew, or if the planners deemed it their duty to "educate" the people to want what the planners wanted them to have, the results of planned production might be most unsatisfactory to the citizens.

Such dereliction from duty on the part of the planners would presumably be short-lived if the government of the socialistic system were truly democratic so that the planners could be removed from office at reasonable intervals if the people were dissatisfied with the results which were produced. However, if the government of the socialistic system turned out to be a dictatorship, so that the planners were safe in their jobs so long as they pleased the dictator or a small group of party leaders, the total results of planned production might be much worse, from the point of view of the needs and desires of the people, than those produced by our capitalistic system. Hence, the question of democracy in government in the socialistic system is a very important one in connection with evaluating the probable results of planned production.

*Efficiency in Production* In turning to the question of the probable efficiency of a socialistic productive system in carrying out planned decisions, we find it difficult to consider the question of efficiency apart from the matter of costs. How can an enterprise determine whether or not it is efficient if it cannot determine the least-cost combination of productive agents for the attainment of a certain result? But land and capital would be owned by society as a whole under socialism and would have only arbitrary accounting costs attached to them. Wages would be more nearly a real cost, but would also be determined arbitrarily and not by the activities of numerous demanders and suppliers in the market. Under these conditions, if the planners could order the production of an economic good by either of two methods, each of which required a different combination of the agents of production, they could never be sure which method should be chosen on the basis of cost. They might

know and prefer the method which produced the greater quantity of product or the method which would give the lowest cost per unit as the planners saw fit to reckon cost, but they could never be sure that the method chosen would actually have involved the least-cost combination of productive agents on the basis of market-determined prices for these agents.

It also seems true that the economic planners would be in a position something like that of one cat watching twenty or thirty rat-holes. The plans would call for certain results to be attained in terms of the production of physical quantities of products, but, if this phase of the plans were stressed unduly, trouble might be encountered with other matters, such as quality of products, labor productivity, the number of workers used, the total wage bill, wear and tear on plant and equipment, inadequate repairs and replacements, or excessive spoilage of materials. It would be a most difficult matter to get everything to come out according to plan, and the planners might well have to choose which parts of the plan were to be completed in full and which should be neglected.

The human element would be an especially important and unpredictable factor in the whole situation. The economic plans would have to predict the activities of millions of human beings, and the planners would never be sure that all these people would behave exactly as they were supposed to in various situations. If the socialistic system proved unable to furnish adequate incentives to individuals, the technical efficiency of productive activities might be seriously impaired. This question of incentives under socialism will be referred to again in connection with the distribution of income.

Even if we disregarded all problems internal to productive enterprises, there would be no reason for thinking that planned productive results could be perfectly attained in practice. Even under economic planning, many phases of production would be subject to the influence of uncontrollable natural phenomena. For example, unusually favorable or unfavorable weather conditions would greatly affect the yield of certain crops and indirectly the output of industries which were dependent on these crops for raw materials. Mines could become flooded, blizzards could tie up transportation for extended periods, and fires could destroy or damage key plants and create bottlenecks. Moreover, wars or even changes in the military outlook could cause the actual results of production to depart significantly from those which had been planned originally, and much

the same thing would be true of technological changes if they were introduced into industry about as fast as they occurred.

Finally, while it might be possible to avoid severe depressions and mass unemployment under socialism, the advantages of a socialistic economy in connection with economic stability would not be nearly so great as they seem at first glance. Consider for example, a case mentioned earlier in this chapter. In the economic plans, the production of coal, coke, and iron ore is coordinated with that of steel, automobiles, tractors, and machinery, but in practice one of the many things which might happen in any economy actually keeps the output of coal and iron ore from reaching anything like the planned estimates. What effect will this have on the steel industry and other industries which require large quantities of steel? It seems clear that these industries will at least temporarily have some unused productive facilities and some unnecessary labor. But, say the socialists, these conditions will not be allowed to spread to other major industries because any necessary price adjustments will be promptly made, and the purchasing power of the workers in the steel industry and other industries using steel will be maintained.

This sounds reassuring, but just what could the socialistic economy do for these workers? It could spread the work in the steel industry and other industries using steel by giving each employee shorter hours of work while maintaining wage payments as before, but something of this sort could be done even under capitalism. If, as seems more logical, some workers were temporarily displaced from the steel industry and other industries using steel, it is contended that there would be no unemployment which would contribute to depressed conditions in other industries because the planned economy would find other jobs for the workers. This it could do, because it would employ workers so long as their products were desired by consumers and not merely so long as it could make profits by using their labor.

But how quickly could other jobs be found for these workers, and what kinds of jobs would they be? If the workers could not be placed in other jobs quickly, the demand for the products of other industries might suffer. Moreover, it might often be necessary to reemploy the workers in jobs in which they would turn out products that, while they would be taken off the market by consumers, could not be produced on the basis of prices and costs, if these prices and costs were freely determined in the market. Such sub-marginal jobs

would prevent unemployment, and it would probably be better to have the workers employed in them than to have them unemployed but the difference between giving the workers employment in sub-marginal jobs under socialism and giving them employment in raking leaves, digging holes, and mending streets under the WPA in our capitalistic system is not tremendous great

All this, of course, does not mean that a socialistic economy would have no advantages over a capitalistic economy in connection with economic stability. Many factors which are important in connection with business depressions and unemployment under capitalism (such as the overexpansion of bank credit in boom periods, the tendency of competitive industries to overshoot the mark with regard to total quantities of productive facilities and the inclination of monopolistic industries to take their losses, when necessary, by maintaining prices and permitting their facilities and workers to be unemployed instead of by lowering prices and continuing to use their productive facilities and labor) would be eliminated or controlled under socialism. However, the fact remains that, until it is possible for planned productive results to be perfectly realized in practice, there are opportunities for grave economic maladjustments to occur under socialism. And, in the face of such maladjustments, it may be held that a socialistic economy would operate to conceal business depressions and unemployment rather than to eliminate them.

All in all, it does not seem possible to predict with great accuracy just how well the total results of planned production under socialism would compare with those produced by our capitalistic system. Certainly, it is difficult to see that there is any great automatic advantage for socialism in this matter. The results of planned production in Soviet Russia do not throw any great light on this matter either, because economic planning in Russia was undertaken under conditions very different from those under which it would have to be attempted in the United States. We do not wish to enter into the controversy as to whether the great backwardness of the Russian economy at the time when economic planning was begun was a great boon or a drawback from the point of view of successful planning. At least this backwardness prevented the Russian experiences with economic planning from being of great value as a guide to the probable experiences of other countries.

*The Distribution of Income.* The socialistic proposition to the effect that the individual citizens should work according to their

desire for compensation and receive income in accordance with the quantity and quality of work done indicates that there will be differences in wages under socialism. However, in the virtually complete absence of property incomes received by some individuals but not by others, it is certain that the degree of inequality in the distribution of income among individuals and families would be sharply less than that which exists in our capitalistic system. In criticizing the proposed distribution of income under socialism, we may admit that many evils which flow from extreme inequality in income distribution under capitalism would probably be eliminated under socialism, and that this result would be desirable. Moreover, the receipt of unearned incomes by individuals would be eliminated under socialism, and this result would also deserve approval. Even under capitalism, most individuals would favor the elimination of unearned incomes as a matter of general principle just as they would favor religion, but no individual under capitalism ever thinks or admits that he personally receives any unearned income. It is always the other fellow's income which is unearned.

The leading question in connection with the socialistic distribution of income is whether the proposed moderate differentials in income would be consistent with the socialist's desire to maintain and expand the total national income. That is, would the small differences in incomes which modern socialism contemplates prove adequate to provide incentives for all? If individuals under socialism would lack incentives to work efficiently, to manage enterprises and industries efficiently, and to invent, contrive, and improve machines and methods of production, the total national income might fall well below that which is produced under capitalism. It is obvious that, if the total national income were too small, it could be divided ever so fairly and equally without producing a high level of economic welfare for the people.

With wages for ordinary grades of labor paid largely on a piece-work basis, it is quite possible that differences in wages at the lower end of the socialistic income scale would be just about as adequate as they are under capitalism from the point of view of providing incentives for ordinary workers. It is far less certain that the modest "upper-bracket" wages proposed by socialists would be adequate to provide incentives for the managers and directors of large-scale governmental enterprises, for inventors and research specialists, and for high-grade professional workers. The socialists

obviously think that moderately large wages for such persons would work out satisfactorily, but this is a matter which can be fully decided only by experience. The socialists contend that individuals, regardless of the difficulty and responsibility of their work, would not mind being only fairly well off, if there were no extremely rich individuals with whom they could compare themselves unfavorably. The socialists do not expect that individuals who had become accustomed to receiving large incomes under capitalism would ever be fully content with the smaller economic rewards available for the same work under socialism. But they expect that as soon as a new generation had come along, composed of individuals who would know nothing about the large differentials in income which formerly prevailed under capitalism, people would work just as hard and efficiently under the small income differentials of socialism as they would under any other system of rewards. However, we have not found these arguments entirely convincing.

In any case, as we have seen, the socialists do not intend to rely entirely on differences in wages to provide incentives for the people. They intend to reduce the importance of economic motivation as much as possible while developing other types of incentives greatly. Among the motivating forces which would be emphasized are such things as power, prestige, public honors and acclaim, pride in work, the joys of creation, extensive opportunities for education and training, jobs well fitted to individual abilities, pleasant and interesting work in advanced positions, the filling of advanced positions on a merit basis, relief from the dangers of social insecurity and unemployment, idealism, altruism, devotion to the cause, and ultimate compulsion and penalties.

Just how well this system of moderate differences in wages combined with a host of other incentives would work out in practice cannot be determined in advance. Fundamentally, the answer depends upon the question of whether people behave acquisitively under capitalism because selfishness and acquisitiveness are an inherent and unchanging part of their nature or whether this behavior under capitalism is produced largely by environmental and institutional conditions peculiar to that system. Of course, many people think that they know the final answer to this question, but they do not agree among themselves very well as to what the answer is. It is our contention that the answer must be obtained from experience in trying to operate a socialistic system. Here again the Russian

experience has not been very helpful. The Russian economy has moderate income differentials and relies on many other types of incentives, and one of its leading weaknesses to date has been low efficiency and productivity on the part of labor of all grades. Other things being equal, this result might point to some deficiency in the Russian system of incentives, but, in the case of Russia, low labor efficiency and productivity could be explained in so many other ways that this conclusion about incentives is not necessarily warranted. Quite apart from the Russian experience, however, it is obvious that, if incentives were inadequate in a socialistic economy, the socialists would have to fall back on their contention that a moderate national income rather equally divided among the people would be preferable to a larger national income divided with great inequality.

**The Population Question** Some critics of socialism contend that the old population bogey might be revived in that system and that population might increase so greatly as to produce very serious consequences. According to this notion, population is held in check under capitalism by the desire of the citizens for economic advancement, since too many children may keep a family from "getting ahead." If a socialistic economy guaranteed jobs at "good" wages for all citizens and undertook to assure support and care for one's children as well as for oneself, families might increase in size so much that standards of living would decline substantially despite our best productive efforts. This criticism lies distinctly in the field of speculation. According to many economists the number of children in a family even under capitalism is often influenced to a considerable extent by noneconomic considerations. Moreover, in our system, the largest families are often found among the most wretched and miserable groups in the population. It would seem possible, therefore, that the assurance of a satisfactory income to all workers might help to hold the population in check rather than to increase it. On the whole, then, we cannot predict that a socialistic system would definitely have a problem of overpopulation.

**The Issue of Freedom** The political and governmental system proposed by modern socialism seems ideal from the point of view of democracy and freedom for the individual, but many questions may be raised concerning the possibility of attaining this ideal political and governmental system in practice. Great difficulties would undoubtedly be encountered in enlightening all the citizens concern-

ing the economic and other issues with which the government would have to deal in attempting to have the government make immediate and precise responses to the changing will of the citizenry, and in handling economic representation and other proposed features of socialistic government. However, the leading question in connection with socialistic government has to do with whether comprehensive economic planning is consistent with political democracy. Full-fledged economic planning seems to require that enormous powers for making and enforcing decisions be centralized in a relatively small group of economic planners near the head of the system. Under capitalism, at least, governmental officials and agencies seldom seem willing to relinquish powers which have once been granted to them and persons in high governmental positions do not always seem willing to give up these positions unless compelled to do so by the workings of the electoral process. If human nature would not be profoundly changed under socialism, there might be grounds for suspecting that the planners would become convinced of their own omniscience as planners and that they would plan above all to keep themselves in office as planners.

Of course, the socialists are not inclined to admit that this danger is very serious. They seem to think that human nature would be so thoroughly changed under socialism that individuals who had been granted enormous powers as planners would cheerfully doff these powers at the end of a short period of years, if their services as planners had not been satisfactory to the citizens. However, it seems to us that the psychological atmosphere under economic planning might not be favorable for the changing of plans and the admission of grave errors in planning, if these changes and admissions were likely to cost the planners their jobs. Since errors would be made and plans would have to be changed from time to time, it seems likely that the planners would try to achieve monopoly powers over their jobs. While admitting that, in theory, economic planning is compatible with democracy, we believe that there is a great danger that economic planning will be associated with dictatorship in practice. And this, of course, would be quite enough to ruin the socialistic system from the point of view of many people.

The socialists admit that various economic rights which are available to the individual under capitalistic institutions would be eliminated under socialism. However, the socialists contend that these rights—such as the right of private property in productive wealth,

the right of freedom of enterprise, and the right to receive extremely large economic gains as the result of exceptional personal accomplishments or the ownership of large amounts of wealth—mean comparatively little to most individuals under capitalism. The individual has these rights under capitalism from a legal point of view, but he is often economically unable to take advantage of them. Under socialism, the individual would retain those rights which are most important to him under capitalism—the right to choose his own occupation out of the many available and the right to spend his money income for any commodities and services which please him.

But we may well ask whether freedom of occupational choice and freedom of consumption choice are compatible with economic planning. It is difficult to see how the individuals of any economic system could have complete freedom in both of these matters at the same time, except in that most improbable case in which the commodities and services which the individuals in the system desired to consume were precisely those economic goods which the individuals as producers desired to turn out. In the usual case, the individuals as consumers will greatly desire some commodities or services whose production is most unpleasant, while some occupations which people would gladly accept as producers will result in commodities or services which the people as consumers do not greatly desire. Of course, some sort of adjustment is achieved under capitalism by means of the relative prices of various commodities and services and the relative wages in various occupations, but the resulting ranges of products and of occupations are never those which the people would have freely chosen on a physical basis.

Under socialism there is the added complication of relating both of these freedoms to economic planning. So what the socialists probably mean by freedom of consumption choice is that the total range of commodities and services which it is deemed worth while to produce will be determined by economic planning, but that the individual consumers will be as free as possible to spend their money incomes for any commodities or services within this range. In similar fashion, the total range of occupations that it is considered desirable to carry on in the economy will be determined by economic planning, but the individuals as workers will have a free choice among all occupations within the socially approved range. Intelligent economic planning will then keep the total range of com-

modities and services and the total range of occupations consistent with each other. Outside of these planned ranges, there will be no freedom at all. No individual will be able to consume yachts or mink coats if these commodities are not included in the planned range of goods to be made available to the citizens, and the individual who wishes to be an adagio dancer or a magician will be similarly out of luck if such occupations have not been provided for in the economic plans.

Thus, it would seem that the individual's occupational and consumption choices, while free within a certain range, would on the whole be strictly limited under socialism. This conclusion is not acceptable to the socialists, who contend that the individual would actually have more freedom in these respects under socialism than under capitalism. In the latter system, there is a tremendous range of consumption choices available on the market, but most individuals have such small money incomes that their actual consumption choices are severely limited. Under socialism, the total range of consumption choices would be more restricted, but, with money income distributed rather evenly among the individuals, each person would be able to purchase and consume virtually anything which planned production made available. Under capitalism, there is a wide range of occupations legally open to the individual workers, but each worker is actually able to qualify only for one occupation or a very small number of occupations. Under socialism, the total number of occupations would be somewhat smaller, but the breaking down of certain environmental barriers to movement between the labor groups by means of education and training would permit each worker to qualify for a broader range of occupations than under capitalism.

*Conclusion.* In evaluating modern socialism as a proposed system, we are faced again with imposing lists of advantages and disadvantages, of assets and liabilities. The socialists clearly have an advantage in supporting their ideal theoretical system in comparison with our actually operating capitalistic system. That is, a system which worked out exactly in accordance with the socialistic model would be regarded by many people as "better" than our actual capitalistic system. On the other hand, the ideal theoretical capitalistic system may well be regarded as superior to any socialistic system as such a system would probably work in practice. While it is clear that modern socialism affords some kind of a workable alternative to

our capitalistic system, the question of just how well a socialistic system would actually operate in the United States in comparison with our existing system of capitalism simply cannot be answered accurately in advance. Apparently most Americans are anxious to postpone any attempt to change our system over to socialism at least until some actually operating socialistic economy is seen to function in a manner which convinces them of the practical superiority of the socialistic form of organization. For the present perhaps the chief objection to socialism is that most of our people simply do not seem to want it.

We shall make no attempt to evaluate in detail the ideal theoretical system of communism. Whether such a system would be desirable if it could be attained might properly be a matter of some controversy, but, for the moment, a more important consideration is that there seems to be no chance for such a system to be attained or to operate in the manner specified in theory. Even those individuals who are enthusiastic about communism as an ultimate ideal concede usually that there would be no possibility of our changing directly from capitalism to communism and admit that a long preparatory interval of socialism would be necessary before we could reach the final goal of communism. In this situation, we may be content with the references which we have already made to the practical difficulties involved in operating a communistic system.

#### QUESTIONS

- 1 "One of the most difficult tasks for socialists in this country is that of convincing the citizens that socialism is desirable." Explain.
- 2 Why should revolution (in the sense of violent overthrow) be avoided if possible, in passing from capitalism to socialism? Explain.
- 3 As a leading socialist you are placed in sole charge of the task of getting productive wealth from private to public hands in passing from capitalism to socialism. What method or device would you use and why?
- 4 Some socialists contend that in passing from capitalism to socialism the capitalistic owners of productive wealth should be compensated by means of "nontransferable, dateless government income bonds, based on present valuation of the wealth but with a low rate of interest." What are the merits of this plan of compensation?
- 5 "The arguments over compensation and confiscation, as methods of getting productive wealth from private to public hands in passing from capitalism to modern socialism are meaningless since both methods actually involve confiscation." Do you agree? Explain.

- 6 "The adoption of socialism, or even the threat of such action, would cause a disastrous exportation of capital from this country" Show whether you agree
- 7 "The total results of planned production under socialism would be better suited to the basic needs and desires of the people than those achieved by capitalistic production on the basis of the market and price mechanisms Why do socialists hold this opinion?
- 8 "Planned production under socialism would be able to achieve a level of technical efficiency higher than that attained under capitalism" Show whether you agree
- 9 "The evils which result from great inequality in the distribution of income under capitalism would be eliminated or greatly reduced under socialism" Explain
- 10 "The great masses of workers would be relatively well off under socialism in comparison with their status under capitalism" What is the basis for this contention?
- 11 Why do modern socialists argue that business cycles would be eliminated in their proposed economic system? Explain
- 12 Would the economic accomplishments of socialism be consistent with the retention of a great degree of political and economic freedom for the individual citizens?
- 13 "A socialistic economy would encounter many problems in trying to adjust planned productive results to the needs and desires of the citizens" Explain
- 14 "The question of democracy in government under socialism is a very important one in connection with evaluating the probable results of planned production" Show whether you agree
- 15 "Under socialism the actual results of planned production could not be expected to be precisely those which were planned" Do you agree? Explain
- 16 "The leading question in connection with the socialistic distribution of income is whether the proposed moderate differentials in income would be consistent with the socialists' desire to maintain and expand the total national income" Explain
- 17 Just how well the socialist system of moderate differences in wages combined with a host of other incentives would work out in practice cannot be determined in advance Why?
- 18 "In actual practice a socialistic economy would operate to conceal business depressions rather than to eliminate them" Show whether you agree
- 19 "Socialism is theoretically compatible with democracy, but there is a great danger that the government of a socialistic economy will be a dictatorship in practice" Explain
- 20 "Socialists promise more than they can deliver when they say that, in their system, individuals will have freedom of both consumption and occupational choice" Show whether you agree

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## CHAPTER 24

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### *EVALUATION OF SOVIET RUSSIA AND SOCIALIST BRITAIN*

WE turn now to the difficult task of evaluating the economic system of Soviet Russia. However, before getting into the evaluation process itself, it may be well to review the factors which make the project so difficult. In the first place, we may note that statistical data on many important economic matters are either unavailable or of questionable value. No general statistics are published on such topics as prices, money in circulation, housing, cost of living, and real wages. Statistics are available on many other economic topics, but the statistics are often given in rubles, and the ruble used in the internal economic activities of Soviet Russia has had an arbitrary and fluctuating value. Many of the ruble figures are supposedly adjusted to allow for the changing value of the ruble, but, in the absence of price-level data, it is impossible to check the adequacy of such adjustments.

The most common source of data on the Russian economy is the Russian government itself (or various agencies of the government), and this is likely to be a biased source. Faced with the task of operating a planned economy in the midst of a more or less doubting and hostile world, it is quite possible that statistics are issued which conceal the failures of the economy and make its accomplishments appear as wonderful as possible. It is all very well to argue that the Russian government needs accurate statistics on all economic matters in order to have any hope of operating its planned economy successfully, but this would not necessarily prevent the making up of a separate and unreliable set of statistics for the education of the outside world. Moreover, different governmental agencies (all supposedly authoritative) often present widely varying data covering exactly the same economic activities in the same period of time.

When we run across five different figures for steel production in 1932, for example, we begin to wonder what the output actually was. And the governmental agencies seldom attempt to correct or even account for the discrepancies in the data which they give out.

Even if we had adequate and reliable statistics covering Russian economic activities, our task would still be complicated by several other factors. The Russian economy has been operating on the basis of economic planning for only a little over twenty years, and it had only fourteen years before its operation was seriously upset by World War II. It is impossible to form an accurate final judgment of its accomplishments and failures on the basis of such a short and interrupted experience. Neither can one evaluate the Russian economy adequately by projecting prewar economic trends into the future. In the past, Russia's planned economy has been handicapped by her backwardness and inexperience with modern productive methods and equipment, but she has had the advantage of being able to take over these methods and types of equipment ready made, instead of having to develop them slowly and painfully for herself.

Russian economic accomplishments on the basis of planning have been very uneven and it is difficult to balance the successes and failures so as to get a general impression. We may suspect, of course, that while a 50 per cent over-fulfillment of plans for automobile production and a 50 per cent under-fulfillment of plans for automobile tire production would balance out to an average of 100 per cent fulfillment, the result would be far from perfect. However, it is not so easy to handle, for instance, a fivefold increase in the number of tractors used in agriculture accompanied by a loss of half the live-stock on Russian farms.

Great as are the difficulties encountered in handling the strictly economic successes and failures of the Russian system, the situation is further complicated by the virtual necessity of giving consideration to some noneconomic factors. Soviet Russia continues to operate under a government which is in fact a strong dictatorship, and her attitudes and activities with respect to such matters as religion and marriage have brought widespread criticism in other countries. On the other hand, Russia has greatly increased the volume of social services at the disposal of the people, has promoted education and the literacy of the people, and has considerably improved the position of women in Russian life. It is most difficult to

know to what extent these factors should be considered as canceling each other and how they should be weighed in relation to the more strictly economic accomplishments and failures of the system. Almost the only ray of light in connection with the problem of evaluation is found in the fact that, on the whole, the final economic goals of the Russian system are apparently not very different from those of our own economy. In both cases, the final goals are apparently found in the maximization of production and of the standards of living of the people, though the two economies disagree enthusiastically as to the institutions and methods which are best adapted to the attainment of these objectives.

*The Nature of the Russian Economy.* Another question which deserves some consideration before we get into the detailed business of evaluation has to do with the exact nature of the Russian economy. From the strictly economic point of view, the economy does not differ very sharply from that proposed by modern socialism. Private property in productive wealth has been almost completely eliminated. Freedom of enterprise exists, for all practical purposes, only for the system as a whole and not for the individual citizens. Economic motivation is played down to a great extent in comparison with the situation under capitalism, and noneconomic incentives are emphasized. Competition is not the ruling force in economic activity. Individuals have considerable freedom of choice with respect to occupations and consumption. Economic activities are operated on the basis of comprehensive economic planning rather than on that of the price and market mechanism. The major fields of industry and business are dominated by public enterprises. Property incomes have been virtually eliminated and inequality in the distribution of income is not so great as that which prevails in capitalist countries. In these respects and in many others, the Russian economy is one of modern socialism.

However, this conclusion would be indignantly denied by many critics of the Russian economy, and the basis for this denial is found primarily in the dictatorial and undemocratic Russian government. According to this point of view, socialism calls for "a planned self-governing management of economic, cultural, and government institutions by the people themselves."<sup>1</sup> On the other hand, in the Russian system,

<sup>1</sup> A. Yugow, *Russia's Economic Front for War and Peace*, p. 256. Reprinted by permission of the publishers.

The dictatorship has deprived the masses of all opportunities of independent participation in the management of industry, it has created a situation in the country in which there is not the slightest hint of public control, no possibility of fundamental criticism of the general policy. An economic system of the Socialist type, i.e. a socialized economy, can develop only when communal life is not shackled, when the labor and the creative spirit of the people are free.

The effect of having a strong dictatorial government extends far beyond the strict field of government itself. According to the critics the elimination of private property in productive wealth has not resulted in socialized property but in property in the hands of the dictatorship, which is a far different thing. All the important economic decisions are made by agencies of the government, i.e., agencies of the dictatorship and not by elective economic organizations or democratic groups of workers. The great masses of people in Soviet Russia as in capitalistic countries are hired employees working for wages. Again, while inequality in the distribution of income in Russia is less extreme than that which exists in our capitalistic economy, it is held by the critics to be much too large to fulfill the ideals of modern socialism. And the chief reason for this condition is found in the dictatorship. The leading members of the Communist Party and of the governmental bureaucracy do not own the productive wealth of the system nor do they receive profits in the ordinary capitalistic sense. But they do control the uses of productive wealth, direct the processes of saving and investment to suit themselves, decide how large a part of the national income the toiling masses shall receive, and are in a position to see to it that their own economic welfare remains at a high level. The gulf between the incomes of these persons and those of the ordinary workers is considerable. Moreover, the lower ranks of governmental bureaucracy are crowded with economically superfluous if not actually parasitic supernumeraries who do not deserve even then relatively more slight elevation above the masses with respect to income.

On the basis of such considerations, many enthusiastic devotees of modern socialism have openly disavowed the Russian economy as an illustration of the type of system which they advocate. But how shall we describe the Russian economy if it is not to be considered socialist? It is obvious from the economic characteristics which we have listed that we cannot consider the Russian economy capitalistic

<sup>2</sup> *Ibid* p. 259 Reprinted by permission of the publishers

in the ordinary sense, and, if the Russian economy falls short of modern socialism, we cannot for a moment consider it to be communistic. Some people think that it is a system of state capitalism, with the leading party members and bureaucrats replacing the former capitalistic class in power if not in ownership, hiring the ordinary workers of the system for wages, and living inordinately well off their exploitation of the masses. However, this description is not particularly satisfactory since there is not really any capitalist class in Russia, nor any market or price system in the ordinary capitalistic sense, and there are no business profits as under capitalism. Still other people hold that the Russian system is inherently similar to that of Germany under National Socialism, and that both systems are examples of a new type of totalitarian economy which defies description on the basis of the old standardized terms. These people, it seems to us, are so completely overwhelmed by similarities between two dictatorial governments and by surface similarities of an economic character that they overlook entirely great differences between Soviet Russia and National Socialist Germany in regard to the social essence and spirit of the systems and the leading goals or objectives which they pursue. In the end, therefore, we shall consider the Soviet Russian system as socialistic, on the ground that it is more nearly socialistic than anything else, although we admit that it falls far short of being a perfect example of the economic system proposed by modern socialism as an idealistic theoretical movement. As Cole says "It is silly to pretend that the Soviet Union is perfect, simply because it is Socialist. But it is even sillier to pretend that it cannot be really Socialist, because it is not perfect."<sup>3</sup>

### *The Accomplishments of Soviet Russia*

In dealing with the subject of production in Soviet Russia, we know that, while the economic institutions of that system differ from our own, the principles and methods which Russia uses in the field of production are for the most part those which we use under capitalism. That is, Russia goes in for roundabout, specialized, and large-scale production in anticipation of demand. The distinctive feature of the Russian productive system is found in the fact that this system operates on the basis of comprehensive economic plan-

<sup>3</sup> G. D. H. Cole, *Europe, Russia, and the Future*. London: Victor Gollancz, Ltd., 1932, p. 31.

ning instead of on the basis of the market and price mechanism. Hence, in this phase of our evaluation, we shall be concerned with the productive results which Soviet Russia has turned out on the basis of economic planning.

*The Continued Operation of a Planned Economy* One general accomplishment with which we may credit Soviet Russia is found in the fact that Russia has been able to keep a planned economy operating and has been able to make considerable economic progress under a planned economy. If this does not seem at first glance to be a wonderful accomplishment, we should remember that, before the great Russian experiment began, there were many people in this and other capitalistic countries who denied loudly that a planned economy could be operated at all or who contended that such an economy, if by chance it did succeed in avoiding complete collapse, must necessarily be stagnant and unprogressive. In the old days, the economist who attempted to describe just how things would be done in a planned economy and just what results would be achieved placed himself in a rather precarious position. He could always be asked to prove his contentions and, in the absence of any country which was actually operating under economic planning, he could never do so to the satisfaction of the objector. Now, at least, we can realize that there is a choice available as between planned and unplanned economic systems. Not only has Soviet Russia been able to keep on operating and make progress under the planned economy, but she was also able to survive the ordeal of participating in the greatest war in history, and this was another feat which many outside observers deemed impossible at the time when Russia was attacked by Germany.

*Methods of Planning* In general, the methods of economic planning in Russia seem appropriate for such an economy and in reasonable accord with the prospectus of modern socialism. The State Planning Commission proper has the assistance of its council, its large staff of planning workers, various statistical, accounting, research, and training agencies, and a large number of subsidiary planning bodies, both functional and regional. The method of making out a tentative plan, submitting it to a variety of subsidiary planning agencies in order to obtain suggestions, criticisms, and counter plans, and then constructing the final plan seems logical. The final plans are detailed, comprehensive, and have reasonable internal consistency, and yet they are flexible and subject to constant

revision. Of course, it may be objected that the State Planning Commission receives too much advice and control from the leaders of the Communist Party and that it pays too little attention to the criticisms, suggestions, and counter-plans received from below. These drawbacks, however, may be attributed largely to the dictatorial form of government under which the Russian economy labors. Under conditions of full democracy, the planning mechanism itself would merit a considerable measure of approval.

*The Elimination of Capitalistic Wastes.* The planned economy of Soviet Russia has been successful, as we should expect, in eliminating many types of waste that are characteristic of capitalistic productive systems. In Russian production, there is no abuse of the profit motive or restriction of the outputs of industries in order to make more money than could be made by maximizing production. Since Russian industries are not organized on a competitive basis, there is no competitive tendency to overshoot the mark with regard to the quantities of productive facilities which are set up in individual industries. The planners make plenty of mistakes in estimating human needs or demands for goods, but once they have reached decisions as to the outputs which are desirable, they do not set up unnecessarily large quantities of productive facilities and then allow a considerable part of these facilities to stand idle because of a deficiency of effective demand. The Russian productive system has not gone in for any undue proliferation of the styles, shapes, sizes, and colors of goods. In fact, any error in this matter has probably been in the other direction. The Russian economy has not devoted large quantities of productive agents to the advertising of large numbers of competitive brands of essentially the same economic goods, and it has not turned its natural resources over to private individuals for wasteful competitive exploitation. The Russian economy has not lived up to the letter of the socialists' proposal of "necessities for all before luxuries for any," but its record with regard to the kinds of goods produced has been relatively good. However, as we shall see, all this does not mean that the Soviet Russian productive system has been free from wastes of all kinds.

*Industrial Production.* The Soviet Russian organization for industrial production is rather complicated and it has been subject to extensive revision from time to time, but the productive results which have been achieved in the field of industry deserve favorable comment on the whole. The rapid increase in the production of

manufactured goods as a proportion of total production under the first three Five Year Plans indicated that very considerable progress was being made toward the planned goal of industrializing the economy. Rapid industrialization and the relatively full use of available productive facilities caused the production of many manufactured goods not only to grow but also to increase several times over. The Russian industrial output increased not only in absolute terms but also in relation to the industrial output of the world as a whole. Finally, the progress of the Russian economy in industrial production was fairly steady and in any case was free from cyclical booms and depressions.

As we have seen, industrial production in Soviet Russia was severely affected by the events of World War II. By dint of strenuous efforts, the production of war goods was not only maintained but even increased to some extent, but the production of goods for civilian consumption fell off very sharply. Russia has spent most of her time since the war in trying to regain prewar levels of industrial production, but the economic plans for 1950 call for much further progress. Some movement toward the goals of 1950 had already occurred by mid 1948.

**Agriculture** The results of the operation of the Russian planned economy in the field of agriculture have not been so favorable as those in the field of industry, but some planned goals have been attained. Russian agriculture was quickly and thoroughly collectivized, that is, in a few years Russian agricultural operations were transferred from private to collective and governmental hands. Since the former peasant organization of agriculture was badly unsuited to the industrialization of the economy and to the general operation of a planned economy, this collectivization was probably necessary and desirable, whatever one may think of the methods by which it was accomplished. The Russian leaders wisely decided to leave a considerable part of the agricultural activities of the country in the hands of collective or cooperative farms instead of insisting that it all be transferred to state owned and state operated enterprises at the earliest possible moment. Other effective devices have been developed for controlling collective agriculture and for keeping its productive results in line with the plans for the rest of the economy.

In the period from 1928 through 1940 the Soviet Russian planned economy also made considerable progress toward another major

agricultural goal—the mechanization of agriculture. Considerable additional quantities of land were brought under cultivation. Actual outputs of farm crops in Russia had their ups and downs, but in many cases improvements in output occurred. In spite of all fluctuations in production, Russia was able to maintain its position of world leadership in the production of several important farm crops and improved its world position with respect to other crops. Many new farm products were developed under planned agriculture.

While the workers on the state farms were very well treated on the whole and while the Russian leaders contended that the income position of the average collective farmer was not too unfavorable in comparison with that of the average industrial worker, it is impossible to state with much assurance that the economic lot of the average Russian farmer improved greatly under the first three Five-Year Plans. On the other hand, most of the sacrifices which were visited upon the Russian farmers were probably necessary to the rapid industrialization of the economy, without which Russia would have had little chance of survival in World War II. Russian agriculture was especially hard hit during the war period and, because of a variety of natural and other factors, has made less progress than other fields of economic activity toward the regaining of prewar levels of production in the years since the war. As a result, the farmers' lot has not been an altogether happy one in recent years.

**Marketing** The Russian system of marketing goods is not yet free from serious defects, but it has made considerable progress over the years of planned operation of the economy. The total volume of retail trade has increased enormously since 1928, as we should expect on the basis of increased outputs of most kinds of goods. Starting with a situation in which widespread and discriminatory rationing existed, in which many types of stores were set up to serve particular classes of people, and in which prices of the same goods varied widely from one type of store to another, the Russian retail marketing system has gone far toward attaining the goal of having a single set of state and cooperative stores selling all types of available goods to all in any desired quantities and at a uniform scale of prices. As we noted in Chapter 11, methods of store operation and levels of managerial efficiency in retailing were highly unsatisfactory in the early days of rationing. In more recent times, many

Russian retail stores have come to offer large varieties of goods, have numerous and well qualified sales people, display and store their goods in efficient fashion, and offer many of the incidental services to which we are accustomed in our capitalistic economy. Moreover, it is claimed that the Russian retailing system now operates with considerable efficiency, since costs for overhead and distribution are said to run well below the average for stores in capitalistic countries. To the extent that this advantage is genuine, it results undoubtedly in large part from the fact that Russian stores are comparatively free from many of the competitive wastes which characterize retailing in other economic systems.

*Credit, Banking, and Investment.* We have found commercial credit to be in widespread use in the Soviet Russian system on the basis of methods which are basically not very different from those used in our capitalistic system, except that the business of commercial banking is a governmental monopoly in Russia and the total volume of commercial credit to be extended is under planned control. It was a difficult task to establish a large scale system of commercial banking and make it operate after the banks had been liquidated during the moneyless period of war communism, but the Russian system of state banking has operated more and more efficiently as time has passed, in spite of a steadily increasing volume of business. The banking system seems well adapted to the needs of a planned economy, and, since the total volume of commercial credit is under planned control, Russia is one country in which the commercial banking system should play no part in causing booms and depressions.

Fundamentally, the process of saving and capital formation is the same in Russia as in capitalistic countries. That is, the process requires that agents of production which might have been used to produce consumers' goods be used to turn out capital goods, and that consumers for the time being must therefore go without consumable goods which they might have had otherwise. The total money income paid to the citizens is more than enough to buy all available finished commodities and services at planned prices, and the government recaptures a portion of this money income for the purpose of capital investment by means of various devices. The funds available for investment are then distributed among industries and businesses by several government banks. The mechanism for handling saving and investment in Russia is just about what one

would expect in a planned economy, and it has certain obvious advantages With both the total amount of saving and investment and the distribution of capital funds and capital goods among industries under the control of the economic planners, many of the problems which are commonly associated with investment credit and banking in capitalistic countries are of no concern in Russia

Saving and capital formation have gone on at a rapid pace and it is commonly estimated that Russia, under the planned economy, has been taking about a third of her national income, on the average and in times of peace, in the form of new productive facilities Thus, Russia seems to have disproved rather thoroughly the common notion that a great volume of saving and capital formation can occur only under capitalism, only when the national income is fairly adequate to start with, and only when the national income is divided very unequally among the individual citizens While the large prewar investment program could be criticized in many ways, it produced results which the planners thought the people and the country needed, and it is difficult to see how Russia could have resisted Germany as effectively as she did if she had not gone ahead rapidly in developing the productive facilities of the country We may also commend Russia's wisdom in decentralizing her new productive facilities and scattering them over the country After being rudely interrupted by World War II, the program of capital investment is scheduled to go forward rapidly under the Fourth Five-Year Plan

*International Trade* The international trade of Russia has been carried on by a governmental monopoly and this trade has always been thoroughly subordinated to the objectives of the national economic plans Russia has made no attempt to import all goods which could be produced more cheaply in other countries than at home or to export only those goods which could be produced more cheaply in Russia than in other countries Too strict a dependence on the principle of comparative costs might have caused Russia to remain a backward agricultural economy, exporting largely raw and partly processed commodities while importing large quantities of finished manufactured goods In order to attain industrialization, Russia has exported at a considerable sacrifice goods which were both inefficiently produced and badly needed at home and has produced at home many types of goods which, at least for a time, could have

been purchased more cheaply in other countries. On the whole, Russia has attained a rather high degree of economic self-sufficiency. We may say in favor of Russia's trade policy only that it has shielded the country to a great extent from disruptive international economic influences and that it has apparently been well coordinated with the long-run goals of the planned economy.

*The Distribution of Income.* In matters of income distribution, Soviet Russia lives up to the specifications of modern socialism at least roughly. With very minor exceptions, property incomes have been eliminated for private individuals. A part of the social income may be construed as consisting of rent, interest, and profits, but this social income, or such part of it as is deemed available for consumption, is distributed to the individual citizens almost entirely in the form of wages. Both wage rates and total wage payments are determined on the basis of economic planning. Differentials in wages between workers exist both for the purpose of rewarding the workers for their differential accomplishments in production and for that of inducing a distribution of workers among occupations and industries which will permit the economic plans of the country to be fulfilled as nearly as possible. On the basis of these differentials in wages, a moderate degree of inequality exists in the distribution of income. Estimates vary as to the degree of inequality which exists in the distribution of the national income. The ratio between the highest and lowest money incomes of individuals has been commonly stated as 10, 12, 15, or 20 to 1, and some critics of the Russian system say that the ratio is more nearly 60 or 70 to 1.

It really matters little which one of these ratios we accept or which one actually exists in the Russian system. Under any of the ratios from the highest to the lowest, it is obvious that Russia has sharply reduced inequality in the distribution of income among persons in comparison with leading capitalistic countries. And, since the differences in money incomes consist almost entirely of differences in wages, Russia may be said to have eliminated almost completely those private incomes of individuals under capitalism which modern socialists regard as unearned. Supporters of the Russian system also contend that inequality in the distribution of real income among persons is less than that which exists in the distribution of money income because of the great volume of social services and free public services which the citizens receive and which are distributed among individuals more or less on the basis of need.

*The Status of Labor.* Since workers are about the only income receivers in Russia, we cannot make the usual comparison between workers and other groups of income receivers. However, there are some grounds for arguing that the status of labor in Russia is generally satisfactory. As we have seen, differentials in wages exist between workers, and these differentials are intended to be adequate to provide incentives for all classes of workers. Wages are on a piece-work basis wherever possible, and the piece rates are supposed to give due regard for the skill required in different jobs. The payment of additional bonuses or premiums for increased quantities or improved quality of output is rather common. Individuals who become "Stakhanovite" workers or "heroes of labor" receive a great deal of favorable publicity as well as fairly large extra economic rewards. The workers are also said to be benefited by such factors as relief from the dangers of unemployment and of economic insecurity in general, and extensive opportunities for advancement. However, as we have seen, the Soviet system does not intend to depend altogether on economic incentives in order to get things done. Reliance is also placed on such things as a great variety of public honors, socialist competition, idealism, altruism, devotion to the cause, pride in the work, the knowledge on the part of the workers that they can benefit themselves by increasing the social product, ultimate compulsion, social disapproval and dishonor in cases of unsatisfactory work, and a variety of fairly severe direct penalties.

Apart from the question of wages and other incentives, the Russian workers have apparently had favorable working conditions in ordinary times. The standard working day has been short in most occupations, and especially short for young workers and for workers in difficult and dangerous occupations. Rest days have been frequent, the workers have enjoyed rather long annual vacations with pay, and the use of child labor has been prohibited. Most Russian workers belong to labor unions, which are of the industrial type. The collective bargaining function of these unions is not of any great importance but they perform a variety of other functions, some of which are not ordinarily undertaken by unions in other economic systems. Russia has a rather comprehensive system of social insurance for its workers. There is no unemployment insurance, since there is supposed to be employment for all in the Russian economy, but virtually all other possible types of social insurance are included. In general, the social insurance benefits provided

by law are rather liberal in comparison with those which are available in most capitalistic systems. Finally, while the real wages and standards of living of the Russian workers and the Russian people in general have remained low in comparison with those enjoyed by the citizens of leading capitalistic countries, there is little doubt that these real wages and standards of living have been slowly and gradually improving, except during the war and immediate postwar periods. And the Russians can at least contend that, if the real income of their economy ever becomes as great on a per capita basis as that of the United States, the ordinary Russian worker will be considerably better off than the ordinary American worker with respect to real income and standards of living because of the much more equal distribution of income among persons which prevails in Russia.

*Economic Stability.* On the basis of the statistical evidence, the claims of modern socialism with respect to economic stability seem to have been fairly well realized in the Russian economy. At any rate, in twenty years of planned operation, the Russian economy has experienced nothing even approximating a severe depression in business and economic activity, nor has there been any troublesome volume of unemployment. While the other economic systems of the world experienced a severe business depression between 1929 and 1932, economic activity in Soviet Russia continued to move onward and upward. Russia is the only important country in the world in which virtually all phases of economic activity were on a higher and more satisfactory level in 1932 than in 1928, and continued progress was made in Russia up to the beginning of the war. The Russian leaders claim, of course, that these desirable results flow from the nature of their system, and, as we have seen, there may be a great deal in the claim that a planned socialistic economy can avoid booms and depressions in economic activity if it strives earnestly to do so. With the constant expansion of economic activity under the Five-Year Plans, the Russian leaders contend that unemployment was quickly eliminated and that Russia has had to struggle with actual shortages of labor of various kinds. If the Russian economy continues to operate according to the principle that workers can always be "profitably" employed as long as they turn out products which are desired by the citizens as consumers, there is no reason why there should be any significant problem of unemployment in the Russian system. Economic plans have not been perfectly made,

or perfectly carried out in Soviet Russia, but the various mistakes and maladjustments have not been allowed to cause business depressions and widespread unemployment.

*The Issue of Freedom.* There is nothing that can be said in favor of the Russian government and political system from the point of view of the freedom of the individual citizen as of the present time. However, if the highly democratic Russian constitution were ever lived up to in practice, the Russian citizens would not have to make any concessions to the citizens of any other country. As might be expected in an economy that is so nearly socialistic from the economic point of view, the individual citizens of Russia do not have various economic freedoms that are ordinarily associated with the existence of capitalistic institutions. On the other hand, the Russian citizens have apparently had a considerable degree of freedom of choice with respect to occupations and consumption, though in these cases the freedom of choice has, of course, been limited to the ranges of occupations and consumable goods that have been provided by the economic planners of the system. This has meant that freedom of choice in consumption has operated within a more limited range than freedom of choice of occupations, for all industries (including those which turn out capital goods) afford a variety of occupations for workers while only the products of industries turning out consumers' goods and services are available for consumption choices.

### *The Failures and Weaknesses of Soviet Russia*

*Difficulties of Economic Planning.* The mechanism by means of which economic plans are made in Soviet Russia seems rather satisfactory on the whole. While the economic planners are subjected to undue influence and control by the leaders of the Communist Party and do not pay sufficient attention to the criticisms, suggestions, and counter-plans received from subsidiary planning agencies and groups, these faults may be attributed to the undemocratic governmental and political system of Russia rather than to the planning mechanism itself. Whether because of the control of the planners by the Party leaders or because of some other factor, many of the goals which were set up for the First Five-Year Plan and even the Second Five-Year Plan were extremely optimistic and incapable of realization, but the plans have gradually become more realistic as experience with planning has been gained.

However, economic planning in Russia has encountered many of the difficulties which were predicted on the basis of theory. Russia has had a price system under the planned economy, but the prices of finished commodities and services and those of the productive agents have been controlled by the same planning authorities who have had to make the most important economic decisions for the economy. In this situation, it is not logical for the planners to use price relationships as the basis for making decisions as to the kinds and quantities of goods to be produced, the allocation of productive agents among enterprises and industries, or the distribution of resources as between producing additional productive facilities and producing for present consumption. There is no evidence that the Russian planners have grappled seriously with what we have called the problem of obtaining a rational allocation of productive resources under socialism or that they have attempted to secure the results of a capitalistic price system without actually having such a system. In the absence of market-determined prices and costs and without any attempt to achieve a rational allocation of productive resources by artificial means, the various important economic decisions have been made rather arbitrarily by the State Planning Commission to the extent that they have not been arbitrarily made for the Commission by the leaders of the Communist Party.

It has been quite possible to make plans in this situation, but there is no reason for thinking that the plans have been perfectly suited to the basic needs and desires of the citizens. Moreover, there has been no way to determine just how good or bad the plans and their results have been on the basis of these human needs and desires. The planners have been able to obtain some idea of the relative intensities of consumer demands for various products on the basis of the planned prices which have been charged, but the very fact that these prices are planned and fixed has impaired the value of this knowledge as a basis for making economic decisions. The market demand for bread, as an example, even at a fixed price will not be the same when other consumers' goods are plentiful and cheap as when these other goods are scarce and expensive. Moreover, the differences in money incomes between individuals in Russia may be large enough so that even a perfect knowledge of effective demands in the market, if the planners had such knowledge, would not furnish a real understanding of the basic subjective desires of the people.

The planners may have provided for the production of a certain quantity of an economic good in a given year, and the entire quantity produced may have been eagerly taken off the market by consumers at a planned price which covered planned cost, but the planners could never be sure that the same quantity of productive resources could not have been devoted to the production of a quantity of some other good which would have provided greater total satisfactions for the consumers Again, in choosing between different methods of producing a given good, when the methods have required different combinations of the productive agents and have been able to produce different amounts of the product, the planners may have been able to justify their decision on the basis of planned prices and costs, but they could never be certain that their decision would have been justified on the basis of market-determined prices and costs In the absence of market-determined interest rates, the planners have had to take a stab in the dark in deciding between more and less roundabout methods of production when the more roundabout method has been able to produce the greater amount of product The planners have had to make their general decisions on saving and capital formation *versus* immediate consumption on the basis of their own ideas as to what the economy needed most They have not been able to determine the wishes of the citizens in this matter at all accurately, nor have they been able to find out exactly by how much their decision missed being coordinated with the desires of the citizens (if, indeed, the planners have cared)

All these difficulties would have been encountered even if all the economic plans had been perfectly realized in practice Actually, of course, the planned results have not always been obtained Uncontrollable natural conditions, technological changes, changing military outlooks and needs, and the sheer unpredictability of human reactions and behavior in given situations have been disruptive factors in connection with plan fulfillment The productive and other results which have actually been attained under the planned economy may have been better or worse than those which would have been attained by a capitalistic economy working in the same general situation There is no way of reaching a decision on this point However, we can see that any superiority of the planned results has been far from inevitable in view of the difficulties involved in planning and carrying out the plans We now turn to

more detailed criticisms of the results obtained by economic planning in the various individual phases of economic activity

*The Results of Planned Production* In criticizing the results of planned production in the field of industry, we may admit the two most commonly made claims of achievement (1) that the Russian economy has been rapidly industrialized and (2) that there were great increases in the outputs of many manufactured goods under the first three Five-Year Plans through 1940. However, both of these achievements are open to considerable criticism. Since the rapid industrialization of the economy has been merely the physical counterpart of the heavy financial program of saving and investment, we shall defer discussion of this matter to a later point in this chapter and shall concentrate attention now on the great increases which have occurred in the outputs of manufactured goods.

*Industry* The great increases in the output of manufactured goods have resulted in large part from the fact that the managers of Russian industrial enterprises have concentrated attention on plan fulfillment in terms of physical quantities of goods to the neglect of other aspects of the plans. Statistics on the outputs of physical quantities of goods tell us nothing about the quality of the goods, and the outside critics and the Russian leaders themselves agree in complaining bitterly about the wretched quality of many Russian manufactured goods. Again, statistics on physical output do not give us any information as to labor efficiency and productivity or costs of production. In general, increased physical outputs of goods in Russia have resulted from the use of increased physical quantities of the productive factors rather than from the increased efficiency and productivity of the agents already in use. By common consent of the outside critics and the Russian leaders, labor efficiency and productivity have not usually increased as rapidly as planned and have remained far short of the levels achieved in other industrial countries. As a result, costs of production of manufactured goods have usually exceeded planned estimates. Some data on these points were presented in our earlier discussions.

Statistics on physical outputs of goods do not show what has happened to plant, machinery, and equipment in achieving the stated results. Obviously, increasing outputs of physical commodities need to be discounted to some extent if they have been obtained at the cost of an abnormal increase in the wearing out and breaking down of machinery and equipment, and the same thing is true of increases

in the production of new capital goods if adequate provision has not been made for the maintenance and repair of old productive facilities. Many reports, including some from official Russian circles, contend that the Soviet planners and industrial officials have been very lax in regard to these matters. The Russian industrial system has apparently suffered from a perennial shortage of good managers, and the planners have had a difficult time trying to provide some force making for business efficiency comparable to that furnished under capitalism by the competition of private interests.

While increases in the physical outputs of manufactured commodities have been common, we should note that nothing like an even or uniform rate of increase has been maintained among the various fields of industrial production. The Russian leaders are fond of stating that individual Five-Year Plans for industry have been fulfilled to the extent of 95 or 100 per cent, but these estimates are based on the values of products in terms of rubles, rather than on physical quantities of products, and it is obvious that fulfillment in terms of rubles may be increased by rises in the prices of products as well as by increases in their physical output. When percentages of fulfillment are computed on the basis of available statistics for physical production, they do not run nearly so high as those announced by the Russian leaders. In any case, there is considerable question as to what average figures or percentages of fulfillment mean, since they cover up great discrepancies in the results produced by individual branches of industrial production. If the machine-building industry fulfills its plan to the extent of 181.2 per cent while steel production reaches only 56.7 per cent, the average of fulfillment in these two branches of production is 119 per cent, but such an average figure seems quite misleading. Such a rapid increase in the output of machinery while steel production is lagging far behind planned estimates would almost certainly cause grave difficulties in various sectors of the economy.

The production statistics also indicate that much greater success has usually been enjoyed in fulfilling the plans for the production of capital goods than in carrying out those for the production of consumers' goods. Since the successive Five-Year Plans have called for greater outputs of producers' goods than of consumers' goods, we could not claim that merely larger outputs of producers' goods than of consumers' goods were any evidence of inefficiency in the Russian planned economy though we might question the judgment of the

planners in this respect. However when, as has often happened according to Russian statistics, the output of producers' goods has actually exceeded the planned estimates while the output of consumers' goods has fallen well short of planned estimates, we are entitled to observe that the Russian industrial system has not even produced the results which it set out to accomplish and that the sacrifices actually made by the Russian consumers have exceeded those anticipated by the planners.

All the considerations just mentioned undoubtedly qualify, though they do not cancel, the accomplishments and progress reported in the field of industrial production through 1940. From 1941 through 1947, further progress toward the goals for industrial production was stymied by World War II. The setback to industrial production during the war and its recovery in the early postwar years just about cancelled out, so that industrial production on the whole had reached approximately the 1940 level by the end of 1947. Further progress in the field had to wait upon the years beginning with 1948.

*Agriculture* In the field of agriculture, we must admit the claims of rapid mechanization and collectivization, but both of these developments are open to serious criticism. Tractors, combines, and other machines used in agriculture have increased in numbers very rapidly except during the war, but mere statistics as to numbers of machines tell us nothing about the quality of the machines, their susceptibility to breakdown, the cost at which they were produced, the availability of repair parts, operators, mechanics, and repair men, or the extent to which the new machines have offset the loss of draft animals on the farms. The collectivization of agriculture was undoubtedly necessary to the operation of the planned economy but we may criticize both the method by which it was produced and the operation of the state and collective farms which resulted. The liquidation of the kulaks was a brutal process involving much loss of life and human suffering. Moreover, according to the critics, the liquidation of anyone who was a little better off than his neighbors meant, in effect, that hard work and initiative were penalized wherever found, the incentives of the remaining peasants were destroyed, and exactly those peasants were eliminated whose skill, knowledge, and industry might have led to the development and improvement of Russian agriculture. The great slaughter of livestock by the

peasants in their resistance to collectivization deprived Russian agriculture of about half of its farm animals.

The state farms proved to be a costly experiment. They have operated at a loss in most if not all years to date, in the sense that they have exceeded their budget estimate of cost while actual income has fallen short of budget figures. They have been roundly criticized for cultivating only a small fraction of their total area, for their high labor and management turnover, for their high personnel costs, and for their excessive livestock mortality. Far too great a proportion of their products has been consumed on the state farms themselves so that relatively little has been available for the market, and there has been much theft and waste in production. It now seems that the Russian planners have abandoned any thought which they may once have had, of converting all or most of the collective farms into state farms.

The collective farms, which are much more important than the state farms on the whole, also come in for their share of criticism. They are said to be so closely controlled by the government and representatives of the Communist Party that they are cooperative in name only. The administration of the farms is often high-handed and arbitrary in its treatment of the individual collective farmers. A fairly large part of the output of the collective farms has actually come from the individual homesteads or plots of land which the individual collective farmers have been allowed to cultivate for themselves. In fact, the managers of the collective farms, in despair over the prospects of increasing truly collective production, have often illegally turned over large quantities of collective land to the individual farm members for private cultivation, in the hope that in this way it would be possible to fulfill the plans for agriculture.

The distribution of income on the basis of "labor days" on the collective farms is complicated, cumbersome, and difficult to apply in agriculture, and it is unsatisfactory from the point of view of incentives since the farmers are likely merely to put in their time and go through the motions. The situation is especially difficult if, as has been alleged, the labor days credited to individual collective farmers depend more on the good or ill will of the farm officials than on anything else. An equal division of income, on the other hand, would have been simple, in line with former practices of the peasants, and a good method of sharing inadequate supplies. In many cases, too much of the income of collective farms has been de-

voted to the construction of community buildings to administrative expenditures, and to actual production expenses, while too little has been divided among the individual farmers. In this difficult situation with regard to positive incentives, the Russian leaders have had to depend in part on negative incentives, and severe penalties are provided for laxity, negligence, refusal to work, crimes (especially theft) against socialist property, and "counter-revolutionary" activities.

The production of leading farm crops in Russia lagged badly under the First Five-Year Plan but showed considerable general improvement under the Second Plan and, in some cases, under the Third Plan through 1940. However, these improvements had to be discounted to some extent because of the adoption of the practice of measuring the crops in terms of biological yield rather than actual yield and because the increased yields could be accounted for to a large extent in terms of increases in the quantity of land under cultivation rather than in terms of increases in the yields per unit of land. By the end of 1947, Russian agriculture had not yet recovered from its wartime experiences, and increases in crops beyond the 1940 levels were still a matter for future years. The results obtained in livestock production have been particularly unsatisfactory. Some progress was made from the low point reached at the end of the First Five-Year Plan, but the goals of the Third Plan were still below those of the First Plan for two important divisions of livestock. Much the same thing is true of the goals of the Fourth Plan, since Russian livestock was decimated further during World War II.

The economic status of the collective farmers remains unsatisfactory. Amid the general rises in prices which have occurred under the planned economy, farm prices have been raised much less than the prices of other commodities, and the purchasing power of farm products in terms of other goods has declined. A considerably greater part of the farm produce reaches the market now than before the revolution, so the farmers have a smaller proportion to consume at home, while on the other hand the rural areas are allotted a far smaller share of the available manufactured goods than they deserve on the basis of population. The large funds used for capital investment in industry are derived to a great extent from the turnover tax in normal times, and the turnover tax on foods and other agricultural products has in some years yielded four times as much

revenue as the turnover tax on industrial products. Thus the turnover tax on agricultural products, which has made up all or most of the difference between the prices received by farmers and prices which these products have commanded on the market, in effect has placed a large part of the burden of industrializing the economy on the agricultural industry. This result is no evidence against the efficiency of the planned economy, since it clearly was intended, but it is frequently criticized on other grounds.

**Marketing** It is perfectly clear that the marketing mechanism in Soviet Russia has improved mightily in comparison with the early days of planning in which many foods and other consumers' goods were strictly rationed, many types of stores served only limited classes of customers, price variations were extremely great from one type of store to another, and methods of operation and levels of managerial efficiency in the stores were highly unsatisfactory. However, in spite of all improvement, the Russian system of state marketing has not been a great success. It has been relatively difficult to transplant modern merchandising methods into the relatively backward Russian economy. A modern industrial plant can be located in a backward area, and, if it is given the latest productive techniques, efficient foreign machinery, and a staff of domestic workers under the control of imported specialists and managers, it has a chance to operate with some efficiency. On the other hand, improved merchandising methods ordinarily develop gradually with the growth of population, expanding transportation and communication, and the slowly changing habits and customs of the people, and it is difficult to introduce modern methods and practices abruptly and still get them to work effectively.

In the second place, it may be questioned whether merchandising (and especially the retailing phase) is as well suited to large-scale management by the government as is, for example, heavy manufacturing industry. If retailing requires quick decisions, flexibility, and ingenuity on the part of store operators, the operation of retail stores on a tremendous scale by the government is almost bound to be awkward, cumbersome, and inefficient. If the prices of certain goods are set too high or too low, great runs on the stores may occur, or tremendous unsold stocks may pile up on store shelves, before the government gets around to change its prices. Supplies of goods sent to the stores are sometimes poorly adapted to local tastes and customs, and goods may pile up in warehouses in some

sections of the country while unsatisfied demands for the same products may exist in other areas Store managers, with little chance for personal gain from the successful operation of their enterprises and under pressure to achieve the planned volume of turnover, are reluctant to stock new types of goods lest these products sell slowly and reduce store turnover

The marketing mechanism in Russia has also suffered because the planners did not or could not see fit to devote large quantities of funds and managerial ability to its development Moreover, it is at the retail level that the problems created by the planners' economic policies (such as rapid industrialization and heavy production of capital goods) come to a head in terms of shortages of consumable goods Even in 1948, the leaders of the Party and government were still greatly dissatisfied with the operation of the merchandising system and were still deciding to take energetic measures which would result in the satisfaction of the legitimate demands of the people for the common necessities of life

*Credit, Banking, and Investment* Both the commercial and the investment banking and credit mechanisms operated under some difficulties in the early days of the planned economy in Russia However, as they operate at the present time, both mechanisms seem rather well suited to the operation of a planned economy, in which it would certainly be expected that the total volume of credit of both kinds and its distribution among enterprises and industries would be closely controlled by the planners On the other hand, the results achieved through the investment credit and banking mechanism have been severely criticized

The Russian economy has gone in for a tremendous program of saving and investment, and this program has resulted in the rapid industrialization of the economy Both the saving and investment program and its physical counterpart—the rapid industrialization of the economy—are usually listed among the accomplishments of Soviet Russia, but there are many offsetting considerations Inefficiency and low productivity of labor have been just as common in the construction of productive facilities as in other phases of productive activity, and the new productive facilities and capital goods often have cost much more than had been planned Much of the capital construction and building has been of low quality in spite of high cost, and the Russian leaders have often included large amounts of unfinished productive facilities in their estimates of

accomplishment in the field of capital construction Russian capital construction has also been afflicted by "gigantomania," or the delusion that, if an ordinary large-scale plant is desirable and efficient, a plant many times as large must be still more desirable and efficient. The search for enormous size has interfered with the completion of construction projects, it has resulted in plants which were too large to be operated and managed efficiently, and it has produced plants so large that they have never been fully operated. The location of the new productive facilities with respect to raw materials and markets has sometimes been unsatisfactory. These criticisms and many others concerning the program of investment and capital construction have been voiced by the Russian leaders as well as by outside critics.

The foregoing criticisms have largely concerned the *efficiency* of the capital-construction program, but criticisms of its *wisdom* have been just as common in the past. Was it wise to construct extremely large hydroelectric plants far beyond the predictable needs of Russian industry when the people of the country were so short of decent housing facilities? Was it wise, in view of the modest accomplishments which Russian agriculture has made, to invest several billion rubles in agricultural machinery and equipment, when finished cotton textiles were extremely scarce and the machinery available for processing raw cotton was inadequate even to care for the existing crops? Was it wise to weight the investment program so greatly in favor of the capital-goods industries? This latter objection does not question simply whether the Russians should have taken so many capital goods instead of consumers' goods for that result is inevitable under any investment program. It questions rather whether the Russians should have taken so many capital goods which will produce more capital goods rather than capital goods which will produce consumers' goods. Such an investment program as was actually carried out inevitably imposed great hardships on the consumers of the Russian economy. Moreover, when low efficiency and high cost have made it necessary either to fall short of planned goals in connection with the investment program or to impose further sacrifices on the consumers of the system, the Russian leaders have never hesitated in selecting the latter alternative.

Hence, it has been contended that the Russians have been trying to starve through to future greatness and in view of the plight of the Russian consumers and the fact that Russian productive facil-

ties still fall far short of those of leading industrial countries such as the United States, it is clear that this future greatness is still to be attained. Every economy should have a healthy regard for future as well as present productivity and welfare, but unbalanced emphasis on the future may be just as unfortunate as unbalanced emphasis on the present, for too great a neglect of consumers' wants in the present may endanger future productivity and welfare. Moreover, when a country goes all out for a capital-investment program, there is always a question as to how useful the enormous quantities of productive facilities are going to be in the future in view of probable changes in technology and in human wants.

It was easy in the years before World War II to criticize the Russian program of investment and capital construction from the point of view of the consumers. Even if the Russian economy had been somewhat successful in getting what it planned in the way of capital construction and development, it could be held that the plans involved treating the Russian consumers very shabbily and that this result was "wrong." On the other hand, the major offsetting consideration is that, if Russia had set out to develop her socialistic economy more gradually, she might not have had any socialistic economy to develop long before now. Russia needed every bit of her newly developed productive facilities in the struggle with Germany. If the planners had decided to give the Russian people more consumers' goods and fewer productive facilities in the past, the people themselves would probably have regretted the decision bitterly soon after the war broke out. In view of Russia's strong stand against Germany, it is now difficult for the outside observer to criticize Russia's decision to stress investment, capital construction, and industrialization as either unwise or unfair. At any rate, Russia is going ahead with a further extensive program of capital investment under the Fourth Five-Year Plan.

*International Trade.* The Russian governmental monopoly in charge of international trade and foreign exchange has followed the policy of gearing Russia's trade into the plans for the development of the national economy. Considerations involving immediate economic gains from importing and exporting have been deemed relatively unimportant in comparison with the major planned objectives of industrialization and independence. In importing what the national economy has needed and exporting only what the planners thought the national economy could spare, Russia's inter-

national trade has not developed rapidly and Russia has achieved a great degree of economic self-sufficiency. The economic costs of self-sufficiency have perhaps not been as great for Russia as for some other countries, because of her wealth of natural resources and great variety of climatic conditions, but no country can completely escape the losses involved in a program of economic self-sufficiency. Russia has been able to obtain a considerable degree of economic self-sufficiency only at the cost of furnishing her citizens with standards of living lower (at least for the present) than those which could have been attained on the basis of geographical specialization and international trade. An indefinite continuation of the policy of national economic self-sufficiency would be unfortunate from the point of view of the Russian consumers, but there is no way to determine at present what Russia's future policy with respect to international trade will be.

*The Distribution of Income.* In the field of income distribution, the main Russian claims of accomplishment require some qualification. The types of private income which the socialists usually regard as unearned under capitalism have been almost completely eliminated according to the Russian leaders, but interest is still paid to individuals on their savings deposits and on government bonds, though these payments amount to an extremely small part of the national income. Moreover, if there are quite a few leading members of the Party and of the governmental bureaucracy who receive large incomes because of their positions rather than on the basis of their functions or productivity, another type of unearned income seems to be present in the Russian scheme of income distribution. According to almost any estimate that has been made, inequality in the distribution of income among persons in Russia is small in comparison with that which exists in leading capitalistic countries such as the United States and Great Britain. However, there are many critics who contend that differences in money incomes in Russia, while they are smaller than those which exist in capitalistic countries, are (1) much greater than the Russian leaders are willing to admit and (2) much too great to be consistent with the ideas of modern socialism.

The critics also contend that the commodities and services which are distributed by the government without charge are distributed in such a way as to increase rather than diminish the inequality which exists on the basis of money incomes. That is, the persons

who draw the largest salaries are said also to be granted the free use of magnificent houses or apartments, country estates, rest homes and sanatoria, expensive limousines, superior educational facilities for their children, and many other things to which the ordinary citizens have no access. Even some writers who view the Soviet system rather favorably on the whole are inclined to lament the fact that inequality continues to exist in the distribution of income among persons and that income has not become distributed in such a way as to produce a classless society. As income is actually distributed, there are obvious clashes of interests as between the peasants and industrial workers, members and nonmembers of the Communist Party, members of the armed forces and the rest of the population, the administrative and technical staff of industry and the ordinary workers, Stakhanovite workers and other workers, and the highly paid artists, musicians, and authors and ordinary workers.

On the whole, however, the distribution of income in Soviet Russia is more often criticized for having too little inequality as between persons than for having too much. According to practically all observers, the major weaknesses of the Russian planned economy have included, among other things, low efficiency and productivity on the part of labor of all grades, including managerial, and the failure to develop loyalty, disinterestedness, and devotion to duty as rapidly as expected. These are exactly what we should expect to be wrong if the Russian combination of economic rewards and other motivating factors were inadequate to provide incentives for all the people. As yet, however, these difficulties may be attributed at least in part to some other factors. Because of the speed with which the Russian economy has been industrialized and mechanized, the Russian labor force in industry (and in some other fields) has been growing very rapidly, and there has never been a time when this labor force as a whole could be considered properly trained and experienced. Russian workers have found it difficult to adjust themselves to the strict regimen of urban industrial life, and they have been inclined at times to be late for work, to miss work altogether if they wanted to do something else on a given day, to take it easy on the job, to disregard safety rules, and to be careless in the use of materials and equipment. Conscious of a general shortage of labor in industry and certain that they could get a job almost anywhere, the workers have been disposed to change jobs frequently and to move from one place to another in search of more favorable oppor-

tunities. The low productivity of other grades of labor has been due in part to the inefficiency of management. All or most of these difficulties may disappear when the Russian planned economy has been operating for a longer time. If they do not, and if labor efficiency and productivity remain low after, for instance, a generation or more of experience with the modern industrialized economy, there will be strong reason to doubt the effectiveness of the Russian system of incentives.

*The Status of Labor.* It is also necessary to qualify rather thoroughly the conclusion frequently reached by supporters of the system that Russia is a kind of workers' paradise. The Russian workers of ordinary grades are fortunate in living in an economic system in which virtually all the income available for consumption is distributed in the form of wages and in which differences between individuals with respect to money income are small relative to those which prevail under capitalism. However, we must always remember that real wages depend upon the total productivity of any economic system as well as upon the way in which the total income is divided. If the national income as a whole is too small, it can be divided with absolute fairness or equality without producing a high level of economic welfare for the individual citizens. While there are grave difficulties involved in estimating the exact income status of the Russian workers, the consensus seems to be that their real incomes and standards of living, although gradually improving up to 1941, remained low in comparison with those of workers of the leading capitalistic countries. During the war and early postwar years, real incomes and standards of living were apparently well below the levels of 1940.

The relatively satisfactory wage rates, hours of work, and other working conditions of Russian labor which existed before the war, as provided by basic laws and decrees, were changed for the worse during the war period, and it now appears that these less satisfactory wartime standards are going to be continued for several years at least in the postwar period. In any case, critics of the Russian system have contended that the wage rates, hours of work, and working conditions specified by laws, decrees, and collective agreements were always meaningless except as a device for deceiving outside observers of the Soviet system. The managers of Russian enterprises were under great pressure to fulfill the plans for production and were subject to severe punishment if they failed to do so. As the lesser of

two evils, they rather openly violated the provisions of the Labor Code and of collective agreements that were based on it. Other undesirable results have come from the attempt to use the piecework basis of wage payment for various types of work which in other countries would not be considered well suited for this system and from certain developments in connection with the Stakhanovite movement.

Made desperate by problems of labor turnover, absenteeism, lateness to work, and loafing, the Russian leaders have imposed conditions on the workers which, according to the critics, amount to virtual enslavement. We cannot repeat here the detailed description of these conditions which appeared in Chapter 17, but they include numerous regulations intended to bind the workers to their jobs, get them to work on time, and keep them coming to work every day. Severe penalties may be imposed for violations of these regulations. Before 1910, these restrictions and penalties may not have amounted to very much, but now plant managers and heads of governmental bureaus who fail to prosecute workers guilty of breaches of labor discipline or who hide workers who are hiding from prosecution as a result of breaches of labor discipline at other plants or bureaus are themselves liable to severe penalties for abuse of power or non exercise of power. Other penalties apply to doctors who show a lack of class consciousness in issuing hospital certificates to workers, and to public prosecutors and judges who have failed to prosecute or punish workers or managers under the various regulations.

It is impossible to deny that most Russian workers are members of labor unions, but the critics allege that the supposed functions of these unions are merely another case of window dressing. The collective bargaining function is said to amount to nothing at all, because wages, hours, and working conditions are strictly determined by state agencies, and the unions never question them. In fact, the unions do not even insist on collective agreements in many cases. The unions are said to be completely unable to protect the workers against summary dismissal, eviction, or imprisonment, against violation of the wages, hours, and working conditions provided by law, or against the violation of safety codes and other protective measures. The cooperation of unions with management means merely that the unions function as slave-drivers, employment bureaus, and collectors of forced loans. They represent the interests of

the ruling bureaucracy and not those of the workers According to this opinion, real labor unions do not exist in Russia today any more than they did in Nazi Germany

Again, we cannot question the existence of most types of social insurance for Russian workers, but criticisms of the Russian system of social insurance are quite numerous Many types of persons are excluded from the social insurance system, and comparatively few persons have been able to obtain benefits up to the present time Those who receive benefits apparently do not get the full benefits provided by law in many cases Since the cost of social insurance has been borne rather directly by the general public, it has been difficult to prevent malingering and other anti-social practices The social insurance benefits have been manipulated in an attempt to prevent or reduce labor turnover The system of social insurance does not include unemployment insurance and it is not altogether certain that we should accept the conclusion that Russian workers are completely free from the danger of unemployment

*Economic Stability* Next, we must return to the popular claim that Russia is a land without business depressions and without unemployment We must admit that the statistics for Russian production, employment, and other phases of economic activity under the planned economy show nothing which could be mistaken for the business cycles that have existed under capitalism However, it would be a sad error to think that economic activity has been perfectly stable in Russia or that it has shown nothing but continued progress Some agricultural crops after five years of planning were below the 1928 and 1913 levels, and the First Five-Year Plan brought a decrease of over one-half in Russian livestock instead of the fair-sized increase which was planned Construction has been held up for lack of cement, agricultural operations have been interfered with by shortages of gasoline, oil, replacement parts, and operators for machinery, plan fulfillments of 181.2 per cent for machine building, 127.2 per cent for other metal products, and 99.8 per cent for fuel have been associated with fulfillments of 56.7 per cent for steel production, 54.2 per cent for the production of cotton textiles, and 86.3 per cent for timber products

These maladjustments are of the type that are likely to cause business depressions under capitalism Under the planned system of Russia, it has been possible to keep the economy running even in the face of such maladjustments and to prevent the most undesir-

able results of business depressions Russia thus has some advantage over capitalistic economies, but her advantage consists not in eliminating serious economic maladjustments but in being able to get along in spite of these maladjustments Russia's experience with the problem of unemployment has been typical according to the critics Russia has not been able to provide full employment for the workers, in the normal sense of "full employment" The serious economic maladjustments which have occurred have thrown many people out of work at least temporarily To be sure, these workers have not been allowed to remain unemployed, and jobs have been found for them, but what kinds of jobs have they been?

It is claimed by the critics that many persons who would otherwise have been unemployed have been put to work at forced labor under miserable working conditions on a variety of governmental construction projects In ordinary industries, large numbers of workers have been employed at extremely low wages and a subsistence standard of living These workers would probably have been unemployed if it had been necessary to pay decent wages, it is argued, for their existing low wages, if paid according to the value of the workers' services, indicated that their products were of comparatively slight value to the economy as a whole Moreover, if and when workers have become unemployed, they have not been allowed to clutter up the streets of the industrial cities Instead, they have been sent back to the farms, and it has been in the form of unnecessary workers on the farms that the unemployment problem has shown itself rather than in the form of completely idle workers, for it is easy to appear to have something to do on the farms

Collective farmers were given plots of land for their own use partly because they were not fully employed on the collective farms proper, and even under the stringent regulations of recent years, the collective farmers have been required to spend only from 80 to 150 days per year in working on the collective farm land This suggests that the collective farms could have operated successfully with much less labor than was actually available for them in most years Thus, it is contended that unemployment has been merely disguised, and not eliminated, in the Russian system in peacetime and that the devices by means of which workers have been given something to do in the Russian system have been somewhat similar to those used for the purpose of "making work" for the unemployed in our capitalistic system In the war and early postwar years, of course,

Russia needed all the workers she had, and more too In ordinary times the Russian system may have some advantages in connection with business depressions and unemployment, but these advantages are not so great as some people suppose

*The Issue of Freedom* Finally, with regard to the question of freedom for the individual, it is difficult to condemn the Russian system too strongly In spite of the democratic facade which the present constitution provides, the government of Russia is a dictatorship of the most absolute and complete variety, with the leaders of the Communist Party in full control The Party dominates the electoral process It maintains Party offices and agencies to match the various officers and agencies of the government The legislature is a mere figurehead It approves the accomplishments and proposals of the Party leaders unanimously and without debate, ratifies automatically any laws desired by the Party leaders, and appoints to all positions within its power such persons as are approved by the Party leaders As if these things were not enough, the Party has at its disposal an elaborate organization for the protection of the regime, including a large and well-trained secret police and laws which define counter-revolutionary and anti-state activities so broadly that almost any acts of the individual citizens may qualify Under these conditions the individual citizens have no rights and no freedom, regardless of what the constitution may say, and especially since the control of the Party extends not merely to economic and political affairs but to such matters as education, religion, and other social institutions as well The Russian dictatorship is the very antithesis of that political and economic democracy which modern socialists expect to have in their ideal system

As we have seen, the situation in the strictly economic field is not much better The individual citizens of Russia are, by the nature of the system, deprived of many of the economic rights which people enjoy under capitalistic institutions The numerous and severe restrictions which have been imposed on Russian workers in recent years indicate that these workers have very little of that freedom of occupational choice which is supposed to be a feature of modern socialism The citizens have more freedom in spending their money incomes, but even here their choice of goods is more restricted than it would be under theoretical socialism On the whole, it is this lack of political and economic freedom for the individual which causes so many people to wonder whether the Russian system should be

described as socialistic, and which causes us to wonder whether comprehensive economic planning and democracy will ever prove to be compatible in any country.

**Conclusion** It is difficult to reach a final conclusion on the Russian system from the available mass of conflicting evidence and argument. Soviet Russia has shown that it is possible for a planned economy to continue operating, to eliminate some of the types of waste and inefficiency which prevail under capitalism, and to make considerable economic progress. On the other hand, Russia has encountered many serious economic problems in operating her planned economy and has clearly demonstrated that not all types of waste and inefficiency are peculiar to capitalistic systems. The supporters of Soviet Russia attribute these wastes and inefficiencies largely to the extreme youth and inexperience of the Russian planned economy. They expect that, in the future, these wastes and inefficiencies will gradually disappear and that the Russian planned economy will improve steadily in efficiency and productivity.

The critics believe that many types of waste and inefficiency are inherent in the nature of the Russian planned economy and will prove as troublesome in the future as in the past. They attribute Russia's progress under the planned economy in the past largely to two factors: (1) the fact that Russia has been experiencing a tremendous building boom, such as the capitalistic countries have had at times, and (2) the fact that the planned economy started with a situation in which the citizens were short of almost all kinds of goods so that they would eagerly accept almost any goods which the planners decided to produce—a situation, in other words, in which almost any planned decisions would seem reasonably correct. And, unfortunately for any hope we might have of testing this point of view, the setbacks received by the Russian economy during World War II seemed to insure a continuation of these two conditions for some years to come. For the present, it seems clear that the Russian system, though it furnishes some kind of alternative to capitalism, is not the kind of an economic system which most Americans would prefer to their own.

### *Evaluation of Partial Socialism in Britain*

**Difficulties of Evaluation** Our evaluation of partial socialism in Britain will be rather brief, for it represents an almost impossible

task at the present time. The Labor Government has been in power in Britain for only a few years, and these years have been a period of transition from capitalism to partial socialism rather than a period of stable operation under a new system. The program of socialization or nationalization of industry is not complete as yet, and even if it were complete it would still be impossible to foresee all its repercussions on the rest of the economy which is supposed to continue to operate under private auspices. Moreover, there is little point in trying to evaluate a system of partial socialism until we have some idea as to whether the socialism can remain partial and whether such a hybrid system can operate successfully. The answer to this question seems far from certain.

Partial socialism in Britain has had no chance as yet to operate in a situation which could be described as reasonably close to normal. The postwar period has been one of continued crisis or emergency. The unbalanced situation in connection with international trade and foreign exchange, the shortages of many kinds of goods, the need for a tremendous volume of industrial and residential construction to repair the ravages of wartime destruction, the need for the modernization of machinery and equipment in industry, the war-weariness of the people, and many other factors have operated to create a trying situation for the introduction of a new system. The Labor Government has considered it necessary in this situation to interfere strongly in most phases of the nation's economic life and to rule the economy with an iron hand. It is not always easy to decide which governmental controls are purely a product of the postwar emergency and which are likely to be continuing features of partial socialism. If we are not careful, we shall be blaming socialism for some controls which would not be necessary outside of the emergency situation or attributing to the postwar economic crisis some controls which are likely to exist rather permanently under socialism.

*Accomplishments of Partial Socialism.* Under the Labor Government, several important industries have been nationalized smoothly and efficiently, and the choice of industries to be nationalized seems sound. The industries were of key importance to the whole economy, had been having difficulties in attaining efficiency in operation and seemed to require radical reorganization along the lines of a centrally operated plan, required large new capital expenditures coming either directly from the state or through state guaranty, and

were already closely linked with other governmental operations. The aims of nationalization are economy and efficiency, and not merely the bringing of some industries under public ownership and operation.

Compensation of the former owners of nationalized industries has occurred on several bases. While it has normally involved the exchange of some sort of governmental securities for private, the compensation has sometimes involved giving the former owners governmental securities to a total value equal to that of the private securities surrendered and in other cases has meant giving them governmental securities which would produce an annual income for the former owners equal to that which they had received on the average over a considerable period of time. In still other cases, where the annual income which the governmental securities would produce was less than that received on the average in the past, it was felt by the government that the former rate of return could not have been maintained in the future under private ownership and operation. While opponents of nationalization sometimes charged that it involved the virtual confiscation of private property, the plans for compensation of former owners of the industries do not seem to have been unreasonable on the whole.

The Labor Government has instituted a most comprehensive program for the attainment of social welfare. The social insurance system is intended to furnish every person with complete social security from the cradle to the grave. Financed by workers, employers, and the state, it provides unemployment pay, sickness pay, maternity and widows' benefits, guardians' allowances, retirement pensions, death grants, children's allowances, compensation for injuries, and complete medical, dental, specialist, and hospital services. Other welfare activities include such things as nutritional programs, furnishing free milk and hot lunches at schools and providing special foods for infants and small children, close attention to factory laws and inspection and industrial health, and a greatly expanded educational and training program.

Apart from the social welfare program, British labor has been treated rather well under partial socialism. Many workers have secured the greatly desired five-day week, hours of work have been reduced on the average, and the government has been much more wary about imposing direct controls on wages than on prices. The Labor Government has also made changes in the tax structure in-

volving reductions and concessions for large numbers of people with small incomes, while imposing heavier burdens on others. Of course, the workers have had to take quite a little governmental control and supervision along with the various favorable developments, but the government has been strongly interested in their welfare.

The Labor Government is apparently determined that Britain shall not again suffer from severe depression and mass unemployment as in the 1930's, and a comprehensive program for the maintenance of full employment has been set up. Prewar depressions had been concentrated to a considerable extent in "depressed areas," dependent on single industries. Under the Distribution of Industry Act, the government has extensive powers to encourage the development of a variety of industries in these areas, now known as Development Areas, and to achieve a better balance of industries in other areas. In this way priority is given to the most urgent industrial needs of the moment and each Development Area is to be built up to withstand any future shocks due to changing industrial demand. Other devices are found in the control of credit policy through the nationalized Bank of England and of the distribution of investment credit under the Borrowing Control and Guarantees Act, and long-range programs of development involving roads, railways, afforestation, ports, industrial plans, new towns, and national parks. Moreover, an economic planning mechanism for the country as a whole has been set up and is in operation.

Finally, the Labor Government has been active and determined in its efforts to cope with the postwar economic emergency. While harassed by rapidly changing conditions which could not be accurately foreseen, it has moved quickly and resolutely to deal with problems as they have arisen. It has not hesitated to cut imports severely, intensify the rationing of scarce goods, control the allocation of labor and other resources, alter its program for capital investments, and order concentration on production for export. It may be that some of the government's actions, seen in retrospect, were ill-advised, but this result is inevitable in such a situation.

*Failures of Partial Socialism.* On the other side of the picture, we may note that productive results under partial socialism have been something less than startling. Production has recovered sharply in a number of industries which operated at very low levels in wartime, but that result would have been expected in any case. Many industries are operating at rates well above those achieved in 1938, but

why would anything else be anticipated by 1948? There has been very little tendency for labor productivity, or output per man-hour or man-shift, to increase either in the nationalized industries or elsewhere, and in some lines of production it may actually have changed for the worse since the war.

In coal mining, for example, the government is inclined to celebrate moderate increases in the total number of workers and in output per man shift, or decreases in former excessive rates of absenteeism, in spite of the fact that the first two of these factors have been running below levels attained in the prewar period while the last factor has been running higher. Moreover, the increase in output per man shift has had to do only with those workers actually engaged in getting the coal out of the ground. But nationalization of the coal industry was followed by a considerable increase in the number of administrative and supervisory employees in the industry, and critics charge that it is greatly overstaffed. In fact, some British newspapers charged that the industry, under nationalization, had provided itself with a staff about the size of the British war office. If productivity were estimated on the basis of the total number of workers in coal mining, it might make a rather dismal showing as compared with prewar results.

Nothing definite can be determined as yet as to what levels of labor productivity will be, either in the nationalized industries or in other fields, under partial socialism. The government is to see to it that the workers have employment, that they have complete social security, that their hours of work are short and their wages adequate, and that their work places are pleasant and safe. It will be interesting to see, as time goes on, whether labor productivity increases under these conditions, as the government hopes it will, or falls away. If labor productivity declines, or can be maintained only by continued severe and repressive controls over the actions of the individual workers, the socialist record will have a long and large black mark on it.

In general the nationalized industries have gone on operating very much as before, but there has been one major crisis involving a nationalized industry. Entering the winter of 1946-47 with abnormally low stocks of coal and with unusually great demands for coal and electricity, Britain encountered exceptionally severe winter weather and heavy blizzards, ice, and gales. Stocks of coal melted away rapidly, and the government had to impose severe restrictions

on the consumption of coal in industries, businesses, and homes, and on all sorts of uses of electricity. The result was not only great discomfort for the citizens but also a sharp and untimely setback for industrial production and reconversion. A considerable volume of unemployment was created, rates of production fell off steeply in many industries, about the equivalent of a full month's output of goods was lost on the whole, and the export program was upset for a long time to come.

This crisis could not be laid completely at the door of the government nor blamed on nationalization, for the bad condition of the coal industry at the time, the unusually heavy demands for coal and electricity, and the severe winter weather would undoubtedly have created a crisis for any government that might have been in power at the time. However, the crisis did emphasize the need for careful planning in the nationalized industries and indicated the dangers involved in taking chances in connection with such a vital industry as coal production. The crisis was the sort of thing that could happen once to anyone. Repetitions of it in the same industry or other important industries might go far toward discrediting the whole program of governmental ownership and operation.

Under partial socialism to date, there has been little if any improvement in the economic lot of the average British citizen. Production in most industries, while increasing, is quite inadequate to provide for both full domestic consumption and the export program, even though imports are drastically restricted. Essential foods and other consumers' goods remain in short supply. Rationing is in force for many articles, and rations are meager. In some cases, they are even below those which prevailed during the war. And the socialist program of austerity, following hard upon the heels of the similar wartime program, has been very difficult for the citizens to bear. Real incomes and standards of living are unsatisfactory, and it is questionable how far these things can be compensated for by expanded programs of social security and social welfare, relative certainty of employment, and shorter hours of work.

The British citizen today is in a peculiar position. He is the beneficiary of a complete system of social security, but he cannot go freely to the store and buy a pound of beefsteak or a quart of milk. He (along with his fellows) owns the coal mines, but he may not own his home if the government decides that it is best for him to live in rental housing made available by the government. He owns

the railways, but he may not ride the highways in his automobile, burning gasoline as he goes. He owns the industry which produces electricity, but he may not keep his electric lights turned on except at such times as the government may specify. If left to make the decision for himself, he might like to have his present situation altered in a number of respects.

Not only does the economic lot of the citizens leave something to be desired, but they are also not allowed to enjoy that life of freedom which they cherished in the past and which the prospectus of partial socialism promised would be continued. Both as individuals or consumers and as business men or workers, they are subject to a veritable flood of regulations that pour forth from various governmental agencies and are harassed by a horde of governmental officials who enforce the regulations. And many of the regulations seem silly or senseless. Why should a person be allowed to burn gasoline in his car to go and fetch a veterinarian to treat his sick livestock but have to walk, run, or ride his bicycle to get a doctor for his sick wife? If he applies for gasoline rations to drive his car to work, on the grounds that the bus will not deliver him early enough, why should a governmental agency, in its infinite wisdom, tell him that he can drive his car to work in the morning but will have to take the bus to get back home at night? Why should he be allowed to order and eat freely food up to the value of two shillings and three pence in some restaurants, but be required to give the names and addresses of the persons who are to eat it if his food comes to two shillings and four pence or more?<sup>4</sup>

In his activities as a business man (or even as a worker), the British citizen is subject to detailed and comprehensive regulation. As we have seen, the government controls by various methods and directly or indirectly such things as production, exports, imports, uses of foreign exchange, prices, wages, rents, interest rates, allocations of credit and investment capital, the allocation and use of materials, supplies, machinery, and equipment, the allocation of labor, virtually all construction activities, and other things. Almost any normal business activity is subject to regulations, and sometimes numerous and confusing regulations with severe penalties for violations. And if by any chance the business man succeeds in making

<sup>4</sup> H. W. Seaman, "Life Under Socialism in Britain," *The American Mercury*, September, 1918, p. 292.

money in spite of all obstacles, a considerable part of it will have to go to the government in taxation.

Sometimes the regulations seem to conflict with each other or with various objectives of the government or even to run in circles. Britain has a shortage of agricultural machinery, which interferes with the attainment of the goal of raising more food at home. But she sells large quantities of agricultural machinery abroad so that other countries can raise more food and sell it to Britain, which cannot raise enough food at home. The government desires to increase agricultural production but issues a regulation stating that anyone who has 50 or more hens must register with the government and sell his eggs to the government at official low prices. So, many people, though willing to keep more hens and produce more eggs, limit their flocks to 49 hens and do not have to comply with the regulation.<sup>5</sup>

*The Permanence of Partial Socialism* It may be objected, of course, that all these regulations and controls over economic activities and the lives of the citizens are due entirely to the postwar economic emergency and would have no place under partial socialism in the long run, but we cannot be sure that this is true. As previously noted, when the present nationalization program is complete, only 20 per cent of Britain's economy is expected to be under public ownership, while the remaining 80 per cent will still be under private ownership and "free enterprise." But is it really possible to divide an economic system into two such compartments and let each go its own way in its own fashion? Will not the operation of one sector of the economy under governmental ownership inevitably have repercussions on the private sector of the economy and modify the results produced there?

If the government absorbs large quantities of savings and invests them in the nationalized industries, as it intends to do, the quantities of savings available for investment in the private sector of the economy, and the interest rates at which they are available, will surely be affected. If the government increases the number of workers used in the nationalized industries, similar effects on the rest of the economy may be anticipated. If certain conditions with respect to wages, hours of work, and working conditions are set up for labor in the governmental sector, the same elements in the status of labor are likely to be influenced in the private sector of the economy.

<sup>5</sup> *Ibid.*

Would private employers be able to treat workers less well than the government does, and would they be allowed to do so in any case? If the operation of the governmental sector is going to affect the private sector in any case, the socialist government is likely to figure that it might as well substitute conscious controls for a policy of letting things find their own level in the private sector.

Another thing to be considered is the policy of the Labor Government with respect to taxation. While granting tax reductions and concessions to large numbers of people with relatively small incomes, the government has placed additional tax burdens on many people with large incomes. As we have noted, the combination of income tax, surtax, and the special levy on investment income will result in total taxes exceeding 100 per cent of income for some persons. If a person had an income of £50,000 in 1948, all derived from investments, his total tax bill on account of the three taxes mentioned would be £69,149, or £19,149 more than his income.<sup>6</sup> While the special levy on investment income is supposed to apply only in 1948, there is always the chance that it might be imposed again and, in any case, one experience of this kind is not likely to be very stimulating to saving and investment by private individuals, most of which is done by persons of considerable means. If private saving and investment is to be discouraged or eliminated, the only alternative is state saving and investment, which will be likely to lead to governmental control, if not outright ownership, of the economy as a whole.

Perhaps the most telling consideration of all is found in the fact that, while 80 per cent of the British economy is supposed to be under private ownership and operation, the whole economy, and not merely the governmental sector, is supposed to operate within the broad outlines of economic plans set up by the government. How can the government get the private sector of the economy to operate according to plan? Private industrialists and business men would probably be glad to follow the plans if the things planned were those which these private individuals would do anyhow, but in such a case the plans would be superfluous and the time and energy devoted to them would be wasted. If the things planned by the government ran counter to the interests of the private enterprisers, it is probable that the plans would be followed only under governmental compulsion. Unless British business men are or be-

<sup>6</sup> *The Chicago Tribune*, April 13, 1948.

come so socially minded that they will follow governmental plans even when these plans are not conducive to their own best interests, it is probable that the government will be able to get the whole economy to run according to plan only by keeping controls on the private sector of the economy which will be similar both in nature and extent to those which have prevailed during the postwar emergency.

It is likely, then, that partial socialism can be made to work only by means of extensive and permanent governmental regulation of the private sector of the economy. However, we may well question whether the Labor Government intends partial socialism to be a permanent system in Britain. It is probable that the Party hopes that its accomplishments in the period prior to the next general election in 1950 will be so great and so well liked by the people that it will be given a mandate to go on to full socialism. Unfortunately, however, the Labor Government may have the economy so well scrambled by 1950 that there will be no alternative except to go on to full socialism, even though partial socialism has worked very poorly on the whole.

Whatever the future may hold, it is certain that opinions now differ sharply as to the merits and demerits of partial socialism in Britain. Mr Herbert Morrison, Lord President of the Council in the Labor Government, for example, is inclined to regard the system of partial socialism as a noble experiment representing the first attempt of a great nation to combine large-scale economic and social planning with a full measure of individual rights and liberties.<sup>7</sup> Mr Winston Churchill, Leader of His Majesty's Loyal Opposition, on the other hand, takes a much more dim view of the whole situation. In calling for the unseating of the Labor Government, he characterized its leaders as unhappy men who "are in the grim and disagreeable position of having promised blessings and given burdens, of having promised prosperity and given misery, of having promised to abolish poverty and only abolished wealth".<sup>8</sup>

Even outdoing Mr Churchill, a journalist wrote in the *Sunday Times*:

The walls of the prison close in day by day, the area of enterprise shrinks. Day by day the ceiling of opportunity is lowered. The prisoners are charged more for the expense of the multiplying jailers. Food and

<sup>7</sup> *Labor and Industry in Britain*, September-October, 1947, p. 155.

<sup>8</sup> *The Chicago Tribune*, October 5, 1947.

drink diminish in quantity and quality month by month. There is no incentive to bold undertakings except a heartless propaganda which urges all dogs collectively to jump the moon while keeping chained each dog with a spring or a heart in him. Socialism, as now interpreted, is competition without prizes, boredom without hope, war without victory, and statistics without end.<sup>9</sup>

In spite of such gloomy pictures, however, we must wait a long time yet before attempting any complete and final evaluation of partial socialism in Britain.

#### QUESTIONS

- 1 Why is it difficult to evaluate the economic system of Soviet Russia? Explain
- 2 "The Soviet Russian economy can be evaluated adequately by comparing its economic accomplishments directly with those of the United States." Show whether you agree
- 3 "The economic system of Soviet Russia is for the most part one of modern socialism." Discuss
- 4 "The planned economy of Soviet Russia has been successful in eliminating many types of waste which are characteristic of capitalistic productive systems." Explain
- 5 Describe the accomplishments of the Soviet Russian economic system in the various fields of production
- 6 "In matters of income distribution Soviet Russia lives up to the specifications of modern socialism at least roughly." Show whether you agree
- 7 "From the point of view of the masses of workers, the economy of Soviet Russia may truly be regarded as a Utopia." Show whether you agree or disagree with this statement, being careful to refer to prospects of employment, social insurance, labor organizations, and wages, hours, and working conditions
- 8 "If the total national income of Soviet Russia ever becomes as great, in proportion to total population, as that of the United States, the average worker would be much better off in Soviet Russia than in the United States." Discuss
- 9 "On the basis of the statistical evidence, the claims of modern socialism with respect to economic stability seem to have been fairly well realized in the Soviet Russian economy." Explain
- 10 "There is clearly nothing that can be said in favor of the Soviet Russian government and political system from the point of view of the freedom of the individual citizens." Do you agree? Explain
- 11 How do the citizens of Soviet Russia fare with respect to freedom of occupational and consumption choice?

<sup>9</sup> Quoted in H. W. Seaman, "Life Under Socialism in Britain," *The American Mercury*, September, 1948, p. 294.

- 12 "Economic planning in Soviet Russia has encountered many of the difficulties which were predicted on the basis of theory" Explain
- 13 Criticize the results of planned industrial production in Soviet Russia
- 14 "In the field of agriculture, Soviet Russian claims of accomplishment are open to serious criticism" Explain
- 15 "In spite of all improvements, the Soviet Russian system of state marketing has not been a great success" Discuss
- 16 Evaluate the Soviet Russian program of investment and capital construction
- 17 "In the field of income distribution, the main Russian claims of accomplishment require some qualification" Explain
- 18 "The distribution of income in Soviet Russia is criticized both for having too little inequality and for having too much" Explain
- 19 "It is necessary to qualify rather thoroughly the conclusion frequently reached by supporters of the system that Soviet Russia is a kind of workers' paradise" Show whether you agree
- 20 "The Soviet Russian system has some advantages over capitalistic systems in the matter of avoiding business depressions and unemployment but these advantages are not so great as some supporters of the system suppose" Explain
- 21 "Partial socialism in Britain offers a particularly difficult problem in evaluation" Why?
- 22 What may we consider tentatively to be the accomplishments of partial socialism in Britain? Explain
- 23 In what respects has partial socialism in Britain to date failed to be a satisfactory system? Explain
- 24 Is partial socialism likely to be a permanent system in Britain? Explain
- 25 How can the Labor Government make plans for the private sector of the British economy and yet expect that these plans will be carried out? Explain

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## CHAPTER 25

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### *EVALUATION OF FASCISM*

OUR study has indicated that the fascist economies were a peculiar hybrid type of economic system. They differed from capitalistic economies over ends or objectives rather than means. That is, the fascist leaders apparently believed that capitalistic economies use good methods to achieve undesirable, or at least relatively unimportant, ends. Private property, free enterprise, and competition are relatively desirable institutions in themselves, and even economic motivation is not undesirable, within limits. The methods and practices of capitalistic production are also appropriate. But all these things under capitalism are directed to the relatively unimportant ends of maximizing production and improving the standards of living and general economic welfare of the individual citizens. According to the fascists, these are not appropriate goals for a nation.

The really desirable goal was considered to be national power, glory, and prestige, to be sought through aggressive warfare and all economic programs, policies, and results were merely means toward the accomplishment of this goal. Therefore, if the economic institutions and methods of capitalism, which fascism retained at least in name, tended to operate, if left alone, to produce results desired by private individuals rather than those which were desirable for the nation, the state (leaders of the government) had to intervene and control their operation in the interests of the nation. Conversely, if the achievement of the aims of the nation led to low standards of living for the individual citizens or involved the enslavement of the workers, these latter results were considered relatively unimportant.

Both in Italy and in Germany, the fascist leaders originally claimed that they had no intention of setting up and operating a fully planned economy. The government was supposed to accom-

plish certain necessary reforms, open up the way for private enterprise and initiative, and intervene directly in economic activity only when private initiative was lacking or inadequate or when the interests of the nation were directly concerned and were likely to suffer in the absence of state intervention. The fascist leaders started out by making a number of friendly gestures in the direction of private business interests, but eventually discovered that the effective pursuit of nationalistic goals and especially the preparation for large-scale war required governmental control over an ever increasing number of phases of economic activity.

The fascist economies operated on the basis of economic planning of at least a rough sort in their later years, although their planning mechanisms were not so well publicized as that of Soviet Russia, and there was apparently no provision for public participation in the work of planning. The plans were carried out not through widespread governmental ownership and operation of industries and businesses but by superimposing a terrific number of governmental controls on what were otherwise essentially capitalistic economies. Governmental intervention and control extended to virtually all phases of economic activity and their effect was to modify profoundly the nominally capitalistic institutions and practices of the fascist systems. However, underneath this thick layer of governmental control, private individuals and firms owned productive wealth, operated the businesses and industries, engaged in competition to some extent, and were motivated largely by the desire for private profits.

#### *The Accomplishments of Fascism*

What can be said in favor of economic systems of the fascist type? In view of the peculiar compromise between capitalism and the planned economy which the fascist countries maintained, it might perhaps be regarded as an accomplishment that they were able to keep their economies operating successfully. Before the fascist countries actually established and operated their compromise economics many people probably would have doubted the feasibility of operating economies of this type. Of course, their operation was successful primarily from the point of view of attaining the ends desired by the fascist leaders, but even that was something. No one can deny that Italy and Germany gained a wealth of experience in operating

their particular type of economic system. Though it is impossible to avoid gaining experience in operating any type of economic system over a period of time and this accomplishment is therefore rather automatic in character, the experience of the fascist countries may be of some value to other countries, even though its value is largely negative. That is, the experience of the fascist countries may be valuable chiefly in showing us what we should not do in attempting to solve our economic problems.

*Productive Results.* In the fascist countries, highly complex governmental organizations were set up for the control of productive activities in general. It was sometimes difficult to ascertain just what functions were performed by various parts of the control mechanism, and there was some controversy as to the results which these mechanisms operated to produce. It is probable that a considerable amount of power and control over production was enjoyed by both business men and industrialists, on the one hand, and by government on the other. However, while there was undoubtedly a certain amount of give and take between private business interests and the leaders of the government in the fascist systems, there can be no doubt that at the absolute top the leaders of the party and government, and the goals which they wished to see achieved, were supreme. No business men or industrialists were big enough to prevail against the dictators and their immediate associates.

With regard to the efficiency with which production was carried on under the fascist control mechanisms, we may say that the increasingly strict control of productive activities by the government probably operated to minimize many of the wastes which are likely to be found in the capitalistic operation of industry. That is, fascist industries were able to avoid to some extent such things as the overexpansion of plant and equipment and duplication of productive facilities, the undue proliferation of styles, shapes, sizes and colors of goods, and the wasteful advertising of many competing brands of essentially the same products. Again, the fascist economies may have had an advantage in that they permitted private individuals to own and operate businesses and industries, bear the risks, and make the profits or losses. This may have furnished better incentives to efficiency than those available under complete governmental ownership and operation.

Finally, there was also a movement toward increasing concentration and combination in business and industry. Many small-scale

businesses were eliminated, while large-scale businesses and combinations increased in number and importance, aided by governmental contracts, subsidies, guaranteed earnings, and opportunities to obtain raw materials at favorable prices. It is likely that the concentration of production in the hands of large-scale businesses and combinations increased the ease and effectiveness of governmental control and may have led to increased efficiency in production. While these developments were offset to some extent by other factors, there is little reason to think that the technical efficiency of productive activities declined under fascism. Therefore, our criticisms of fascism in connection with the control of production must deal to a great extent with the nature of the objectives which were set up for and accomplished by fascist industries and businesses rather than the efficiency which was shown in pursuing these objectives.

The fascist economies were prompt in recognizing the existence of an agricultural problem in their midst, and many steps were taken for the announced purpose of affording relief and assistance to the hard-pressed farmers. Some of the fascist agricultural policies may have been of some benefit to individual farmers or groups of farmers, but the economic lot of agriculture as a whole did not improve significantly in the fascist countries. In any case, the agricultural policies were probably motivated not so much by any love for the farmers or any desire to benefit them as individuals as by the desire to bring agriculture to a condition in which it might be expected to hold up its end of the general program for attaining national objectives of economic independence and preparedness for war, and, in Germany, by the desire to extend the fascist racial program and policies to the farms. The fascist agricultural policies may have contributed something to the attainment of the national goals approved by the fascist leaders, but not much more than that can be said for these policies.

Activities in the field of exchange were brought under governmental control by means of the same general mechanisms which were provided for controlling other productive activities in the fascist economies. In addition, the economic policies which the fascist countries were following in their pursuit of announced national objectives made it necessary to introduce strict rationing of large numbers of consumers' goods and severe measures for the control of prices. While both rationing and price control may have pro-

duced a more equitable sharing of burdens and sacrifices than would otherwise have existed and while both may have made the lot of the ordinary consumer better than it would otherwise have been under the other economic policies of fascism, there is little to be said for either policy on general economic grounds. These policies, at best, were merely consistent with the other economic policies of fascism and with the national goals which the leaders were seeking.

In both Italy and Germany, various reforms were carried out in the field of commercial banking, and the activities of the commercial banks were brought more closely under governmental control, but changes in the field of investment credit and banking were much more revolutionary. Dividends which corporations were allowed to pay on their securities were strictly limited. The earnings which the corporations were thus compelled to retain might be invested in the same lines of production if the corporations were producing articles which were of importance under the self-sufficiency or armaments programs. Otherwise, the government would "persuade" the corporations to invest their earnings in new plants which would contribute to these programs, or in government bonds which would place the funds directly at the disposal of the government for the same purposes. New security issues on the part of private industrial and business concerns were severely curtailed, and private firms were made to look to the government for investment funds. Firms producing ordinary consumers' goods were not allowed to sell new securities, could not obtain additional investment funds from the government, and under price control were unable to acquire large earnings of their own for purposes of reinvestment. Thus, the entire investment-credit mechanism was brought under the thumb of the leaders of the government, and investment funds were diverted into fields of production which were deemed consistent with the attainment of national objectives.

Both fascist countries experienced severe difficulties in the field of international trade after 1929, because their imports of vital foods and raw materials had to continue, and it was impossible for them to dispose of their customary volume of exports. As a result, all manner of controls were applied to imports, exports, and the use of foreign exchange. The devices which were used included tariffs, import and export licenses and quotas, export subsidies, private-trading agreements, clearing agreements, payments agreements, direct-barter deals, and other things. However, neither country

maintained a very large volume of international trade on the basis of these controls and both turned to comprehensive programs for achieving national economic self-sufficiency. The self-sufficiency programs included increasing the production of articles already produced in the fascist countries in amounts inadequate for domestic needs, attempting to substitute articles which were relatively less scarce for others which were relatively more scarce, and producing artificial substitutes for articles which could not be produced in the fascist countries by natural methods. There are obviously no direct gains in terms of maximizing production and standards of living to be obtained from the curtailment of international trade and the development of national economic self-sufficiency. The most that can be said of these policies, as of other fascist control policies, is that they were apparently consistent with the national goals of independence and readiness for aggressive warfare.

*The Distribution of Income* In the fascist countries, the distribution of income remained distinctly of the capitalistic type. With productive wealth privately owned and most industries privately operated, individuals were allowed to receive rent, interest, and profits as well as wages and salaries. There was no tendency for the proportion of the national income going into wages, salaries, and other earned compensations to increase in relation to the proportion going into profits, undistributed profits, interest and dividends, and rent. In fact, the tendency was in the other direction, at least in Germany, and inequality in the distribution of income increased. There was no feature of the distribution of income in the fascist countries which could be regarded as an accomplishment of fascism unless it was that great inequality in the distribution of income among persons was not allowed to accomplish all its usual undesirable results, since large portions of the incomes of all classes of persons were taken by the government for its own purposes.

*The Status of Labor* There is not much that can be said in favor of the status and general treatment of labor in the fascist countries. To be sure, industrial peace was maintained to an unusually great extent, and this is one feature of fascist economic operation which commended itself to certain business men in the United States and other capitalistic countries. The workers were permitted to have organizations of a sort, systems of social insurance were maintained, the paternalistic governments at least nominally protected the workers against some of the most rapacious activities of the em-

ployers the "dignity" of the workers' position was said to have been increased, and the Dopolavoro and Strength Through Joy movements provided a variety of activities to occupy the minds and bodies of the workers in their spare time. No bouquets can be handed to the fascist countries in connection with the wages, hours, and working conditions of labor or real wages and standards of living, so in the end we must fall back on our usual bromide to the effect that the treatment of labor in the fascist countries may have been consistent with the general program for the attainment of national objectives. And the same thing is all that can be said for their policies for stimulating the growth of population.

*Economic Stability* Skipping over the question of political and economic freedom for the individual in connection with which no claims of accomplishment can be made for the fascist countries, we arrive at the question of economic stability. The experience of Italy in the severe post-1929 depression indicated that up to that time the control policies of fascism had not been able to solve the problem of securing economic stability. However, in the process of preparing actively for total war and carrying on war itself, both Italy and Germany were able to achieve, if not economic stability, at least a rather steadily increasing level of economic activity and relatively full employment of labor and other productive resources. This in itself was not a very wonderful accomplishment since the same results can occur in capitalistic countries under similar circumstances. However, with their economic systems under complete governmental control and operating on the basis of economic planning of a sort, the fascist countries (if their fascist systems had survived the war) should have had an advantage over ordinary capitalistic economies from the point of view of avoiding business depressions and unemployment.

If we have not been able to construct a very imposing list of the accomplishments of fascism, it has been because we are unable to accept the fascist notion that the goal or objective of a country should be the attainment of national glory and prestige by means of aggressive war. Anyone who was able to accept such a national objective as desirable would have a much more favorable opinion of fascist accomplishments, since the fascist organizations and policies were, in the main, consistent with the attainment of this objective. Apart from this, the accomplishments of the fascist countries were not at all noteworthy.

*The Failures and Weaknesses of Fascism*

**Productive Results** In turning to a discussion of the failures and weaknesses of the fascist systems, we must remember that most of the questions with which we shall deal were not failures and weaknesses from the point of view of the attainment of the national objectives of fascism. In fact, the fascist leaders would have regarded many of these things as evidences of success or at least as inevitable and rather unimportant accompaniments of success. That is, our criticisms will allege that the fascists accomplished many results which we regard as undesirable and failed to accomplish many results which we regard as desirable. Fundamentally, they will be criticisms of the fascist objectives rather than of the success with which they pursued their objectives.

In the field of industrial production, the rather complete governmental control which developed in the fascist countries may have resulted in the elimination of some of the competitive wastes of capitalism, but any such advantage was offset by the development of bureaucracy and red tape, countless forms and regulations, bribery, "wangling," and the necessity of worming into the good graces of fascist officials. The tendency toward industrial concentration and combination may have improved the economic position of the surviving enterprises besides simplifying the problems of governmental regulation and control. However, any joy which large business men in the fascist countries may have experienced at being relieved of their smaller competitors must have faded rapidly as Party members themselves went into business and used the powers of the one-party state for their own economic aggrandizement. The economic successes achieved by these Party men were extraordinary and the increases in their wealth and income were compared with the loot and booty of the feudal robber barons.

On the whole, however, there is little reason to think that the technical efficiency of production was lowered significantly under fascism and it may actually have improved. Thus, our chief criticism of the fascist control of production rests on grounds of ethics rather than efficiency. While the fascist industrialists and business men were expected to bear the risks and responsibilities of running their enterprises and were supposed to be motivated by the prospect of profits, they were severely controlled by the government and deprived of most of the economic freedoms under which the private

operation of business may be expected to be successful and satisfying. On the other hand, it was unfortunate from our point of view that virtually all increases in the total production of the fascist economies were directed toward economic independence, armaments and war rather than toward increasing the real incomes and standards of living of the citizens.

In agriculture, the fascist policies of price control and cooperative marketing under strong governmental supervision may have afforded at least a partial solution to the famous "scissors problem," or the disparity between the prices received by farmers for their products and the prices of industrial goods and other products which they buy. On the other hand, the farmers as a whole cannot be thought to have gained greatly from participation in the programs of economic self sufficiency or from the programs of land reclamation carried on by the fascist governments. No really determined attack was made on many fundamental farm problems such as tremendous concentration in the ownership of farm land, farm tenancy, and the great disparities in income and economic welfare which existed between the poor and prosperous farmers. In Germany, the extension of the racial program to agriculture and the attempt to form the farmers into a definite and permanent caste tied to the land seemed particularly deplorable.

As a matter of principle, there is something to be said for strict governmental control over commercial and investment banking activities, if not for actual governmental ownership and operation in these fields. Either device might eliminate or greatly reduce the significance of the various economic problems which are found in these financial fields in our capitalistic system. However, in the fascist countries, governmental control of commercial and investment credit was directed toward the goals of national economic independence and readiness for war almost exclusively and not toward the maximization of the economic welfare of the people. In the field of exchange and marketing, the general results of fascist control policies were similar to those produced in industry, but here we also encountered the devices of rationing and price control. The rationing of foods and of consumers' goods of many other kinds may have served to distribute the burdens and hardships, produced by other fascist economic policies, fairly equitably among the citizens. However, the rations made available to the people inevitably resulted in very low standards of consumption, and we must remember that

these burdens and hardships would not have been necessary if the economy had not been geared to the objectives of national economic independence and war. The attempts at price control were undoubtedly necessary and desirable in view of the other economic policies which the fascist countries were following, but the efficiency of the mechanisms for controlling prices left much to be desired. As we have seen, many devices for circumventing and undermining price control were developed in both countries and the effective stabilization of prices occurred only in the official statistics of the fascist governments, despite the severe penalties which were provided for violations of the price decrees.

The fascist leaders of both countries sometimes contended that their policies for severely controlling and limiting international trade and for securing national economic self-sufficiency were thrust upon them by the economic conditions which existed in the world after 1929, but this conclusion was at best only partly valid. In the absence of the program of planning and preparing for aggressive warfare, the difficulties with respect to international trade and foreign exchange which the fascist countries experienced in the post-1929 depression could probably have been overcome, and the great sacrifices involved in the development of economic self-sufficiency would not have been necessary. The nature of the costs of economic self-sufficiency was rather obvious. Attempts to increase the production of articles which were formerly produced in inadequate quantities in the fascist countries could be carried out only at sharply increasing costs of production, and they often involved a curtailment of the production of other things which were also badly needed. Attempts to substitute relatively plentiful materials for relatively scarce ones in production may have resulted in increased economic independence, but they certainly produced unsatisfactory results in other respects. In general, the artificial substitutes were higher in cost or lower in quality (or both) than the natural products which they replaced, and some of these substitutes had special qualities which made their use in industry difficult or required larger quantities of machinery and equipment than would have been necessary to process the natural products. The production of artificial substitutes required the construction of much costly plant and equipment, and the funds for this purpose were derived to a great extent from the old-established industries of the fascist countries. As a result these ordinary industries found it difficult to maintain and renew their

own productive facilities and the quantity, quality, and cost of their products were often adversely affected. Finally, the production of synthetic materials, while bringing increased economic independence in some sectors of the economy, sometimes caused shortages in other sectors.

All or most of these factors had a most unfortunate effect on the real incomes and standards of living of the citizens of the fascist countries. However, the results of the economic self-sufficiency program should not be considered as any evidence of inefficiency on the part of the fascist countries in attaining their objectives. The objectives were self sufficiency and preparation for war, and the countries were rather successful in reaching them. The fascist leaders never claimed that they were going to improve the real incomes and standards of living of their people, to increase the quantity or improve the quality of goods available for immediate consumption, or to cause the old-established industries producing consumers' goods to flourish and prosper. We criticize the fascist leaders not for failing to get what they wanted but for paying so little attention to the presumed fundamental needs and desires of the people.

*The Distribution of Income* Any notion that there was anything socialistic about fascism was quickly dispelled when we observed the distribution of income in the fascist countries. In Germany, and probably in Italy too, the proportion of the national income going to property owners and business enterprisers in the form of rent, interest, and profits increased under the auspices of fascism, while the proportion going to the workers of the countries as wages, salaries, and other types of compensation for productive labor decreased significantly. Moreover, inequality in the distribution of income among persons increased instead of diminishing. Economic inequality was kept from becoming completely intolerable only by the fact that the government's need for revenues for its own purposes placed a severe drain on the incomes of all classes of income receivers.

*The Status of Labor* The status of labor in the fascist countries seemed deplorable from what the fascist leaders would have called our "outmoded and archaic capitalistic point of view." In both countries, wage rates fell sharply in the depression years after 1929. In the following years of economic revival, wage rates advanced only slightly from their depression lows, though total wage payments increased as the result of increased production and more

hours of work. Still later, under price control, wage rates were stabilized at their existing unsatisfactory levels. Thus, the money wages of workers in the fascist countries remained very low and they were subject to many types of taxes and other deductions. Even before the outbreak of World War II, the fascist countries did not succeed in raising the real wages and standards of living of the citizens significantly from the low levels which had prevailed during the great depression, and, in the years of actual war, these real wages and standards of living declined materially.

A considerable degree of industrial peace was obtained in the fascist countries but only at great cost to the workers, if not to the employers. The workers had no labor organizations worthy of the name. The organizations to which they had to belong were really government inspired and controlled organizations, headed by Party men and interested primarily in seeing that the interests of the nation (as the fascist leaders saw them) did not suffer as the result of anything that went on in the field of industrial relations. The workers had no real right to bargain collectively with their employers, they were allowed to use none of the weapons of industrial conflict to bring their demands forcefully to the attention of their employers, and the wages, hours, and working conditions which were so important to them were determined, except for the supervision and intervention of the government and its agencies, by the fiat of the employers and at their pleasure. The employers were also deprived of their usual private organizations, they were called upon to give up their tried and true weapons and practices of industrial conflict, and they were subjected to many burdens by the government and the Party. However, except for governmental intervention, the employers still held the upper hand in their direct dealings with the workers because of their natural superiority of bargaining power. The equal treatment of parties unequal in strength still left them unequal in strength. And there is no certainty whatever that the interests of the workers were adequately protected by the Labor Courts, Courts of Social Honor, and the other elaborate devices which were set up for this purpose, although the fascist leaders attributed impressive records to some of these agencies.

Apart from the matter of wages, the situation of the workers of the fascist countries with respect to hours of work and working conditions in general was not favorable even in the years before

the beginning of World War II, and in later years the situation of the workers became steadily worse. The famous (or infamous) work books or labor passports, the conscription of workers of almost all kinds, the freezing of workers in their jobs, the application of military or semi-military regulations to the workers, and the suspension of former legal restrictions and limitations on hours of work and other working conditions were all part of the order of the day in the fascist countries. As compensation, the workers had the benefits of the Dopolavoro and Strength Through Joy movements (and, in Germany, the Beauty of Work movement as well). However, the workers had almost no freedom of choice or conduct in their leisure-time activities and they were the "beneficiaries" of a strong program of political education in these activities, which means that plays, movies, concerts, operas, courses of training, lectures, and other activities were all "coordinated" with the fascist philosophy. In the long run, the workers themselves did most of the paying for the activities of Dopolavoro and Strength Through Joy, and these activities were regarded by the fascist leaders in part as a means of keeping the workers out of mischief in their spare time. The activities were intended also to keep the workers reasonably happy and contented, so that they would be easier to govern and more productive in their work.

The workers were also compensated in part by the systems of social insurance which the fascist governments maintained. However, in Italy, many persons were excluded from some of the types of social insurance, the benefits received by the insured were pitifully inadequate, and the cost of the insurance was borne to a great extent by the workers themselves. In one year, the expenditures for social services made up less than 1 per cent of total governmental expenditures, and the social insurance funds in general paid out in benefits only a relatively small fraction of their receipts. In Germany, the workers also paid heavily for their social insurance, the payments of benefits for various social insurance purposes were changed considerably under fascism, the government was very niggardly, on the whole, about increasing total expenditures for all social insurance purposes, and the program as a whole may be regarded as rather inadequate.

Finally, the workers were compensated perhaps by the joy which they found in realizing that they were an important part of a national community which (according to the fascist leaders) was con-

stantly growing in power and importance According to these leaders, the main issue with the workers was not their ridiculous wage-pennies, but the dignity and honor of their position Or, as Dr Robert Ley said, in comparing the German worker to a soldier,

Formerly the soldier received 20 pfennigs By this was clearly meant, "Your work as a soldier I cannot pay you for, nor does the Fatherland attempt to pay you for it What it does do is provide you your nourishment, clothing, and physical well being Precisely in this sense are you a soldier!" And a soldier has honor Does the officer seek to drive a bargain with the soldiers, and the soldiers with him? Unthinkable! But the power of command is not enough The greater the power of command, the greater must be the responsibility you bear It does not mean to be the sole master in one's own house in accordance with civil ideas of arbitrary power, but it means to be a leader, to see to it that one knows and cares for every individual, molds the human beings, leads every individual in a truly inner sense The question who will pay for it is ridiculous and irrelevant The question is "Is the principle right?" Do you [the workers] want to be a business commodity or a soldier with honor? I ask the business man, does he want to be a calculator and a financier, or an officer? Then everything is clear and there are no more questions<sup>1</sup>

Perhaps we should emphasize again that these developments in connection with the status of labor under fascism were not to be regarded as failures of the fascist economies to produce the results which the leaders were seeking In fact, the treatment of labor under fascism may be considered as reasonably consistent with the attainment of the national objective of fascism Certainly the fascist leaders never promised the workers the right to belong to unions of their own choosing, the right to collective bargaining and the weapons of industrial conflict, high wage rates, short hours, and completely satisfactory working conditions, or improved real incomes and standards of living On the other hand, we are free to criticize the status of labor in the fascist countries as unsatisfactory from the point of view of our own notions of the objectives which an economic system should seek to reach

*Business Depressions and Unemployment* In the last decade of fascism the fascist leaders took many bows for their success in maintaining an ever increasing volume of productive activity in general in their countries and in eliminating the problem of unemployment Both countries were severely afflicted with unemployment in 1932, but in a few years they converted an unemployment problem into

<sup>1</sup> Quoted in W R Deuel, *People Under Hitler*, p 305

one of labor shortage In later times, these countries had to place increased reliance on women workers They called aged workers out of retirement, relaxed former restrictions on the employment of Jews, recruited workers from the prisons, drove many workers from handicraft and itinerant trades into industry and business, and even employed large numbers of war prisoners However, as we have seen, it is no great feat of economic magic to achieve an expanding total of economic activity and employment in wartime or even in a period of active preparation for war And we do not know how effectively the completely government-controlled fascist economies could operate under ordinary peacetime conditions Theoretically, they should have an advantage over ordinary capitalistic economies from the point of view of avoiding business depressions and unemployment, but we cannot be sure that the fully controlled fascist economies would even constitute a tolerable form of organization for peacetime conditions Of course, Italy operated under fascism for several years under peacetime conditions, but governmental controls over the economic system had not then developed to nearly their later level

*The Question of Freedom* From the point of view of freedom for the individual, there was almost nothing to be said for the fascist countries The government in each case was a complete dictatorship, with the fascist party and its leader in absolute control Party members held almost every office of any importance, and there was a striking duplication of personnel between the governmental officers and agencies and the matching officers and agencies maintained by the party The electoral process was first controlled and then almost completely eliminated, so that most governmental offices were filled by appointment from above The legislatures became mere figure-heads and practically all laws were made by executive decree The court systems were "purified" and filled with loyal fascists Law practically ceased to exist as an objective concept, since it depended on the changing will of the "leader" and his henchmen Elaborate organizations, including secret police and special courts, were set up for the protection of the régime and the party, and laws covering offenses against the state were so loosely worded that it was possible to punish the individual for almost anything he did The power of the party extended not only to the national government but to the district and local governments as well And the fascist leaders claimed that all this was not only necessary but also desirable

According to the fascist philosophy, sovereignty lies in the state and not in the individual citizens. The state is everything, the individual is nothing. Individuals are insignificant particles in the long life of the nation, they cannot even be conceived of as existing apart from the nation as a whole, they have no interests which may be regarded as superior to those of the nation, and they have no rights which the nation is bound to respect. When this philosophy was carried out in practice, the status of the individual was deplorable. In the fascist countries, freedom of speech, freedom of the press, freedom of assembly, and most other civil rights of the individual were completely eliminated. The education of the individual was brought under party control. Teaching staffs were "purified," education was restricted largely to boys, textbooks were rewritten, and racial and political subjects were emphasized in the curriculum. Scientists and research workers were made to give up their search for absolute truth and to devote their talents to producing "fascist truth." Great masses of the most ridiculous party propaganda were thus enabled to masquerade as bodies of scientific conclusions. In Germany, even religious freedom was virtually destroyed by party controls over the churches and the clergy.

The effect of all these events was a really tragic spiritual impoverishment of the individual. In the absence of freedom of speech, or any real public opinion, or any genuine critical judgment of public policies, the people were led to celebrate their own enslavement and to engage in debasing hypocrisy and servility. Economic or political success was made to depend on boot licking, apple polishing, or even bribery instead of real effort and achievement. Initiative and responsibility were weakened. True scholarship and original creative thought disappeared. The young people of the fascist countries were prostituted to the purposes of the state, their mental development was blighted, and they were brought up to worship blindly the things that they had. However unfortunate the lot of the ordinary individual may have been, his position was infinitely worse, at least in Germany, if he were unfortunate enough to be a Jew. The National Socialist racial program involved persecution and brutal violence to an extent which beggars description. The racial program would have been bad enough on any grounds, but it seemed even worse to the extent that it was based on the ridiculous myth concerning the Nordic or Aryan race and its alleged superiority. However, as we have seen, the real reasons behind the program

of anti-Semitism seem to have been the necessity for a scapegoat or bogey-man on which all misfortunes, domestic or international, could be blamed, and the desire to transfer Jewish wealth and jobs to "deserving Germans."

The status of the individual in strictly economic matters was not much better than it was in these other fields. The business man or enterprise in the fascist countries nominally had a certain amount of freedom of action, but in actual practice he was tied hand and foot by governmental controls. For the ordinary individual, freedom of occupational choice, or indeed almost any freedom of action as a worker was virtually destroyed. The freedom of choice of the individual as a consumer was severely limited by rationing, price control, and the productive results of fascist policies with respect to economic self sufficiency and war. Surely no one could approve of the fascist systems from the point of view of freedom for the individual unless he could agree with the fascist leaders that "the maximum of liberty coincides with the maximum of state force."

**Conclusion** From the economic point of view, fascism involved the imposition of numerous and severe governmental controls on what was otherwise a capitalistic economic system. These controls were intended to insure that the results produced by the economic system would be those considered appropriate by the leaders of party and government from the point of view of national goals and objectives. While few of us, as citizens of a capitalistic system, would have much use for any economic system which operated under complete governmental control, it may be said that the fascist system of economic control did not compare unfavorably with other systems of complete governmental control from the point of view of the technical efficiency of production and management. In other words, if we could approve of the national objectives of fascism, we might say that the fascist system of leaving the risks and responsibilities of operating economic enterprises to private individuals and stimulating these individuals by means of competition and the prospect of private profit, while making sure by means of governmental controls that the total economic results produced were appropriate, might produce better results on the whole than the Russian system of outright governmental ownership and operation. Indeed, the fascist control methods differed only in degree rather than in kind from governmental controls which are sometimes employed under capitalism.

Apart from our dislike of the completeness of governmental control over economic activity under fascism, our chief criticism concerns the nature of the national objectives of fascism. It seems that the general goal which the fascist countries were seeking—attaining national power and glory by means of economic and aggressive warfare—is both monstrous and injurious. Rather doubtful that the most persuasive of leaders could have the people of the fascist countries full of devotion and enthusiasm for such an objective if the government had been democratic and responsible to the people. This seems especially true in view of the extremely serious economic consequences which the policies adopted in pursuit of this objective had for the people as individuals. As a matter of fact, the objective in question was forced on the people by a strong dictatorial government which controlled almost every phase of the lives of the individual citizens and deprived them of virtually all their liberties.

And what did the people of the fascist countries receive in return for all their economic hardships and suffering and for their loss of civil, political, economic, religious, and practically every other kind of liberty? Judging from the events of World War II, fascism in Italy was unable to produce even an economy and a nation which was strong in war. In Germany, on the other hand, an effective war economy was unquestionably developed, but it was entirely inadequate for the task of world conquest without which most of the gains which immediately resulted from military conquest could not be retained. On the whole there seems to be nothing about fascism which should lead us to consider it as a desirable alternative to capitalism.

#### QUESTIONS

- 1 Describe the general nature of the fascist economic systems.
- 2 "It may perhaps be regarded as an accomplishment that the fascist countries were able to keep their economies operating more or less successfully." Explain.
- 3 "The economic accomplishments of fascism in Germany and Italy were for the most part those which will be obtained rather automatically by any country which tries to operate under a new kind of economic system." Do you agree? Explain.
- 4 "There is little reason to suppose that the technical efficiency of productive activities declined under fascism." Show whether you agree.

- 5 "Criticisms of fascism in connection with the control of production must deal primarily with the objectives which were set up for and accomplished by fascist industries and businesses" Explain
- 6 "The most that can be said for fascist policies and methods in the various fields of production is that they were apparently consistent with the national aims of the fascist leaders" Explain
- 7 Some American fascists say "The fascist economies of Italy and Germany had a definite and important advantage over our capitalistic system in that they eliminated labor problems and industrial conflict" Evaluate this opinion
- 8 "Fascist economies should have some advantage over ordinary capitalistic economies from the point of view of avoiding business depressions and unemployment" Explain
- 9 "All or most of the fascist policies and methods in the various fields of production had a most unfortunate effect on the real incomes and standards of living of the citizens" Explain
- 10 "Criticisms of the fascist economies must turn largely on ethical questions rather than questions of efficiency" Explain
- 11 "The list of failures and difficulties of fascism in Germany and Italy coincides almost perfectly with the list of fascist economic policies" Show whether you agree
- 12 "Any notion that there was anything socialistic about fascism is quickly dispelled when we observe the distribution of income in the fascist countries" Explain
- 13 "The status of labor in the fascist countries seemed deplorable from what the fascist leaders would probably have called our 'outmoded and archaic capitalistic point of view'" Explain
- 14 "From the point of view of freedom for the individual, there was almost nothing to be said for the fascist countries" Explain
- 15 "The experiences of the fascist countries demonstrated that national economic self sufficiency is indefensible except as a war policy" Do you agree? Explain
- 16 You are selected to give an address to a group of people who believe that socialism, as practiced in Russia, and fascism, as practiced in Germany and Italy, are in reality the same thing though called by different names Explain the arguments which you would use in trying to convince these people that there are significant differences, from an economic point of view, between these two types of systems



**P A R T I I**



*Marxian Socialism*



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## CHAPTER 26

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### *THE MARXIAN PHILOSOPHY AND INTERPRETATION OF HISTORY*

FOR many people, no treatment of the "isms" or of comparative economic systems would be complete which did not deal at some length with the subject of Marxian Socialism. The work of Karl Marx has literally been all things to all people. His works have indicated to some people that he was one of the most brilliant and penetrating economists who ever lived, but the same writings have convinced other people that Marx was a crackpot and a fool. To different people, Marx's writings appear both naively idealistic and hopelessly materialistic. In some places in the modern world, Marx's doctrines appear so dangerous and so completely antithetical to the truth that their study is proscribed, while in other places any serious deviation from the Marxian analysis comes under the heading of rank heresy. In part, the difficulty lies with Marx's writings themselves rather than with their readers, for his writings are often vague and ambiguous. He frequently skimmed over matters which should have been strong points in his analysis only to overdevelop favorite minor points of his own. His style is often heavy and abstruse, and his reasoning complicated and inconsistent. Moreover, he never did present in reasonably brief compass in any one place a complete statement of his position on economic matters.

However, there is no disputing the great importance of Marx's writings. His doctrines form a large part of the theoretical foundation of modern socialism and communism, and attempts to refute these same doctrines have given more orthodox economists a great deal of "busy work" through the years. Even the modern fascist philosophy is constructed in part as a refutation of some of Marx's leading doctrines. In view of the abusiveness and inconsistency of Marx's writings, the business of interpreting Marx or of explaining

"what Marx really meant" has long been one of the most popular of indoor sports. We have not included Marxian Socialism in the main body of our work on comparative economic systems because Marx's writings dealt largely with the description, explanation, and evaluation of capitalism as he saw it and with predictions concerning its future development and eventual downfall. When it came to the treatment of the ideal economic and social system which would one day replace capitalism, Marx dealt largely with general outlines and did not go into details extensively. However, now that our analysis and evaluation of economic systems, both theoretical and actual, has been completed, we may properly spend some time with the Marxian analysis. First, however, we need a few words on the life of Marx.

*The Life of Marx.* Karl Marx was born of Jewish parents in 1818 at Treves (Trier) in southeastern Germany. His grandfather, and other ancestors in preceding generations, had been rabbis, but his father was a lawyer who had many clients but was not especially successful at making money. His father was converted to Christianity and was baptized when Karl was in his sixth year. Marx attended the elementary schools of his native town, spent a year at the University of Bonn, and then attended Berlin University ostensibly to study law. However, after the death of his father in May, 1838, Marx devoted himself primarily to philosophical studies and hoped to attain a lectureship at the University of Bonn through the good offices of a friend, Bruno Bauer. He received his doctor's degree from the University of Jena in 1841 on the basis of his thesis entitled "On the Differences between the Natural Philosophy of Democritus and Epicurus."

His lectureship at Bonn failed to materialize and Marx became a free-lance journalist. In 1842, he became editor-in-chief of the *Rheinische Zeitung*, a daily paper founded by a group of Cologne business men. This paper was soon suppressed by the government and ceased publication in March, 1843. In spite of his uncertain prospects, he was married on June 12, 1843 to Johanna Bertha Julia Jenny von Westphalen, daughter of Baron von Westphalen. After about five months of honeymooning and intensive study at Kneuznach, Marx was called to Paris to participate in the publication of the Franco-German Year Books, which were intended to be an international organ of liberalism. The publication collapsed after its first issue, but Marx remained in Paris for fifteen months, continu-

ing his studies and literary work. In August, 1844, he began his lifelong friendship and collaboration with Friedrich Engels, socialist son of a wealthy cotton manufacturer. Engels contributed a great deal to Marx's thought and writing, and he also contributed heavily later on to the financial support of Marx and his family.

Marx's radical literary activities led the Prussian government to ask for his expulsion from France, and he was duly expelled in January, 1845. With assistance from Engels, he was able to find refuge in Brussels, where he remained until the outbreak of the French Revolution in February, 1848. During his stay in Brussels, Marx continued his study and his output of communist propaganda, but he also wrote one important book, *Misère de la Philosophie* (1847), and a shorter work entitled *Wage Labor and Capital*. Late in 1847, the Federation of the Just (Communist League) engaged Marx and Engels to prepare a statement of principles (party platform) and the result was the justly famous *Manifesto of the Communist Party*. Marx went to Paris in 1848 on the strength of news of the French Revolution, but stayed only until June, and then went back to Germany in company with Engels. There they published the *Neue Rheinische Zeitung*, a highly radical paper which was suppressed in May, 1849. After brief stops in Frankfurt and Paris, from which he was once again expelled, Marx found permanent refuge in London.

Except for a brief visit to the United States, Marx remained in London for the rest of his life. He continued to write for various newspapers and at one time was a European correspondent of the New York *Tribune*. However, he derived much of his support from a legacy received from a friend and from an annual stipend which Engels, then in business in England, provided for many years. He continued his intensive studies of economic affairs, and he is said to have spent ten years in incessant study in the British Museum before publishing the first volume of his three-volume work, *Das Kapital*, which appeared in 1867. In these years in England, he also wrote *The Critique of Political Economy, Value, Price and Profit*, and many other works, but he did not live to publish the last two volumes of *Das Kapital*. These were constructed by Engels from Marx's extensive notes and were published in 1885 and 1894. Marx also represented German workingmen at an international conference in London in 1864. When the International Workingmen's Association, or "First International" was formed, Marx was an active

participant and drew up a statement of its principles He remained more or less active in this organization until it collapsed in 1876 Marx is now remembered not for his journalistic or revolutionary activities but for his writings on economics and capitalism He died in 1883, a little more than a year after his wife's death.

### *The Marxian Philosophy*

***The Philosophy of Hegel*** As we have seen, Marx was always greatly interested in philosophy, and under other circumstances he might well have been a professor of philosophy at some institution of higher learning He examined intensively all types of philosophy which came to his attention in an effort to find a system of philosophy which would fit his own notions and fill his own needs, but no existing system of philosophy seemed entirely satisfactory The philosophy which suited Marx best was that of the German philosopher, Georg William Friedrich Hegel (1770-1831) One of the leading principles of the Hegelian philosophy was the idea of constant change That is, the only unchanging thing is change itself, or, as Hegel put it, the only immutable thing is the abstraction of movement The whole world, indeed the entire universe, is constantly changing Nothing is completely permanent, but everything is continually evolving, developing, becoming

Moreover, according to Hegel, reality existed only in the world of ideas Objective things and events are of no importance The only thing that matters is what we think about these objective phenomena The real universe is one of ideas, and change therein is the only real change Thus it would seem that if an objective phenomenon has changed, but we think that it has not changed, then in reality no change has taken place In similar fashion, if a material object or condition has remained unchanged but we think that it has changed, then in reality change has taken place While it would not always be very safe to act in practice on the basis of this principle, it was strenuously advocated by Hegel The chief task, therefore, was to explain the method by which change occurs in the world of ideas

The Hegelian dialectic, or explanation of the method by means of which change occurs, involves the concepts of *thesis*, *antithesis*, and *synthesis* A particular thought or idea which we have and use is known as a *thesis*, but no idea can exist without an opposite,

which seems to contradict or quarrel with it. Thus, it would be impossible to have an idea of "light" unless we had one of "darkness." The opposite idea is known as the *antithesis* or negation of the original idea. In the realm of the human mind, there are numerous theses and antitheses. The constant tendency is for conflict or struggle to exist between thesis and antithesis, and from this struggle a new principle or idea results, which is known as the *synthesis*, or negation of the negation. However, according to the principle of constant change, this synthesis or new idea will be held and cherished only until it attracts or creates a new opposing idea or antithesis to struggle with it and create a new synthesis, and so on and on. This universal and never-ending process was thought to explain completely all phenomena within the universe (which, of course, was one of ideas).

Another illustration of Hegel's dialectic method is his conception of human history, which he regarded as the progressive embodiments of the world spirit striving with man for the realization of divine ideals. According to him, the physical universe is now a practically finished creation, in which there is incessant motion but very little change, whereas historical development is relatively rapid, and there can be seen the struggle for higher and higher human values such as patience, duty, order, justice, freedom, and love. This self realization or revelation of the divine thought and will is gradual but progressive because of the fact that every partial truth has a beneficial opposition or contradiction in itself, an antithesis which negates the inadequate idea and leads to the negation of the negation in a higher and truer synthesis. In the words of Hegel, "The dialectical principle constitutes the life and soul of scientific progress, the dynamic which alone gives immanent connexion and necessity to the body of science. Wherever there is movement, wherever there is life, wherever anything is carried into effect in the actual world, there dialectic is at work. Contradiction is the very moving principle of the world."

The fundamental principle of Hegel's dialectical idealism, "nothing is identical with itself, but everything contradicts itself," is decidedly evolutionary and progressive, and yet susceptible of revolutionary interpretation. But Hegel was quite conservative in his attitude toward the changing world, as may be seen in his celebrated dictum, "Whatever is real is rational and whatever is rational is real," the implication being that the absolute reason or spirit or God is revealing Himself in human history as fast as possible, and that under any given conditions of time and place the world is good. And yet, according to his own philosophy he might as truly have said, "Whatever is real is irrational," since whatever is has within it contradictions that will make it more rational. So also Hegel could say with equal truth "Whatever is is right," and "Whatever

"is is wrong" But he stressed the former truth, and for that reason it has been said by Engels and other revolutionists that there is a fundamental contradiction in his system between his revolutionary dialectics and his socio political conservatism<sup>1</sup>

*Marxian Modifications and Limitations* As we have said, Marx approved of much of the Hegelian philosophy The idea of constant change as the dominant characteristic of the universe seemed to him a profound truth and he gladly accepted the Hegelian dialectic involving thesis, antithesis, and synthesis as a good explanation of the method by means of which change occurs in the universe However, he could not agree with the idealism of Hegel which involved the notion that reality existed only in the world of ideas and in the mind of man and that the struggles or conflicts which produced change were conflicts of ideas In criticizing Hegel on this point, Engels said

While materialism conceives nature as the sole reality, nature in the Hegelian system represents merely the "alienation" of the absolute idea, so to say, a degradation of the idea In all circumstances thinking and its thought product, the idea, is here the primary, nature the derived element, which only exists by the condescension of the idea And in this contradiction they floundered as well or as ill as they could<sup>2</sup>

But Marx did not propose to do any floundering in an idealistic philosophy For him, reality was found in objective events and phenomena, not in mental concepts The thesis and antithesis whose conflict produced change were objective material forces existing in the universe, and not merely conflicting ideas, and the resulting synthesis was again an objective phenomenon Thus, for idealism Marx substituted materialism As Marx himself put it

My dialectic method is not only different from the Hegelian, but is its direct opposite To Hegel the life-process of the human brain, i.e., the process of thinking which, under the name of "The Idea," he even transforms into an independent subject, is the demiurges of the real world, and the real world is only the external, phenomenal form of "The Idea" With me, on the contrary, the ideal is nothing else than the material world reflected in the human mind, and translated into forms of thought I therefore openly avowed myself the pupil of that mighty thinker, and even here and there, in the chapter on the theory

<sup>1</sup> J. E. LeRossignol, *From Marx to Stalin* New York Thomas Y. Crowell Company, 1940, pp. 95-96 Reprinted by permission of the publishers

<sup>2</sup> Friedrich Engels, *Ludwig Feuerbach* New York International Publishers, 1935, p. 28

of value, coqueted with the modes of expression peculiar to him. The mystification which dialectic suffers in Hegel's hands by no means prevents him from being the first to present its general form of working in a comprehensive and conscious manner. With him it is standing on its head. It must be turned right side up again, if you would discover the rational kernel within the mystic shell.<sup>2</sup>

Marx proceeded to turn the Hegelian dialectic right side up and to study its working in the ordinary events of the world of human affairs.

In speaking of objective events and phenomena as reality and of their reflection in the human mind, Marx appears to consider the human mind as relatively unimportant. It apparently is a shallow thing, like a mirror, which is capable of reflecting external phenomena but nothing more. Our thoughts are controlled by the events of the external world, and we cannot possibly avoid thinking as we do in a given environmental situation. Thus an employer of labor after the Industrial Revolution and development of the factory system would have thoughts concerning his workers which were quite different from those entertained by an employer of labor several decades before. When the environmental situation is ripe for the development of a certain idea, principle, or theory, the appropriate mental concept will be developed, perhaps by one man and perhaps by several. In support of this notion, one might refer to the many cases in which the same theory or even the same mechanical invention has been developed independently by two or more individuals living in different countries and apparently completely unaware of each other's work. However, this interpretation of the human mind would not be very flattering to Marx himself. His thinking and writing would have to be considered a necessary and almost automatic product of the environmental conditions which prevailed in the middle years of the nineteenth century. And it could be argued that, if Marx had not thought and wrote as he did, someone else would almost inevitably have done so.

Some supporters of Marx, however, strongly deny that he meant to assert the supremacy of matter over mind. According to this view, his intention was merely to show that the mind "works by embodying itself in things, changing their shape and potency, and combining them into relations and systems whose changing phases

<sup>2</sup> Karl Marx, *Capital*, Volume I. Chicago: Charles H. Kerr and Company, 1906  
p. 25

are the basis of the history of mankind" <sup>4</sup> Marx would not have denied that the things which he described as material and as forces of social evolution are more and more products of the human mind as time goes on. Marx's interpretation of events is called "materialistic" only to distinguish it from the "metaphysical idealism" of Hegel and his immediate followers. As a matter of fact, it is said, Marx did not raise the issue of mind *versus* matter at all. He "upheld actual mind equally with actual matter against the Absolute which was greedy to engulf them both" <sup>5</sup>.

In any case, we must realize that the Marxian philosophy is as universal in its application as that of Hegel. That is, it constitutes an explanation of realistic phenomena and events in all fields and must be considered to include the mind of man as one part of the phenomena existing in the universe. However, Marx did not attempt to make applications of his philosophy in a large number of fields, but instead limited his use of it to the field of social institutions and processes. This in itself should not be considered as a criticism of Marx, for it would be impossible for a single individual to apply his philosophical interpretation intensively to more than a fairly limited field of phenomena. But in cultivating his chosen field, Marx reached a conclusion which was in no way necessary on the basis of his general philosophy. He concluded that, in the field of social institutions and processes, one type of phenomena contained greater potentialities for producing change than any other. These phenomena were found in the economic field. Basic theses, antitheses, and syntheses were economic in character, and developments in other fields of human relationships were dependent upon changes in the economic sector. Finally, on the basis of his philosophy, Marx could not accept the conservative outlook of Hegel, which more or less approved conditions as they were. Marx was interested in changing things as well as in explaining them. His philosophy was dedicated to revolutionary change and his dialectic was meant to be a weapon for use in the struggle against the existing economic and social order.

### *The Marxian Interpretation of History*

*Marx's Objective* The Marxian interpretation of history follows rather closely on his basic philosophy, but before we pursue the

<sup>4</sup> G D H Cole, *What Marx Really Meant* New York Alfred A Knopf, Inc, 1937, pp 11, 12, and 16 Reprinted by permission of the publishers

<sup>5</sup> *Ibid*

matter further we should see why Marx was anxious to develop an explanation of history. In general, his purpose in seeking the explanation of past history was to become able to predict future events. He knew that he did not like the capitalistic system as it existed and he thought that, if he could discover what had brought the system to its present stage of development, he could predict its (probably horrid) future fate. If he could understand the forces that had caused past events, he would have knowledge of the forces which would cause future events. Furthermore, he thought that knowledge, in this case as in so many others, is power. If we can understand the future events which the forces already at work in our social system are tending to produce, we may be able, by skillful and timely intervention, to influence these future events and mold them nearer to our heart's desire. As Engels put it

Active social forces work exactly like natural forces blindly, forcibly, destructively, so long as we do not understand and reckon with them. But when once we understand them, when once we grasp their action, their direction, their effects, it depends only upon ourselves to subject them more and more to our own will, and by means of them to reach our own ends. When once their nature is understood, they can, in the hands of the producers working together, be transformed from master demons into willing servants.<sup>6</sup>

The Marxian interpretation of history was intended to be a means of making history and not merely one of explaining it.

*The Nature of the Interpretation* The Marxian interpretation of history holds that the stage of economic development or mode of production is the determining factor in the field of social relations and processes. When the mode of production undergoes any significant change, the result is to produce changes in social institutions, laws and legal relationships, government and political institutions, and even mental processes and habits of thought. As Marx himself stated the case

I was led by my studies to the conclusion that legal relations as well as forms of state could neither be understood by themselves, nor explained by the so called general progress of the human mind, but that they are rooted in the material conditions of life. The general conclusion at which I arrived and which, once reached, continued to serve as the leading thread in my studies may be briefly summed up as follows. In the social production which men carry on they enter into definite relations

<sup>6</sup> Friedrich Engels *Socialism Utopian and Scientific* New York International Publishers, 1935, p. 68

that are indispensable and independent of their will, these relations of production correspond to a definite stage of development of their material powers of production. The sum total of these relations of production constitutes the economic structure of society—the real foundation, on which rise legal and political superstructures and to which correspond definite forms of social consciousness. The mode of production in material life determines the general character of the social, political, and spiritual processes of life. It is not the consciousness of men that determines their existence, but, on the contrary, their social existence determines their consciousness. At a certain stage of their development the material forces of production in society come in conflict with the existing relations of production or—what is but a legal expression of the same thing—with the property relations within which they had been at work before. From forms of development of the forces of production these relations turn into their fetters. Then comes the period of social revolution. With the change of the economic foundation the entire immense superstructure is more or less rapidly transformed. In considering such transformations the distinction should always be made between the material transformation of the economic conditions of production which can be determined with the precision of natural science and the legal, political, religious, aesthetic, or philosophic—in short ideological forms in which men become conscious of this conflict and fight it out.<sup>7</sup>

In other words, economic activity is the fundamental basis of human life. As Engels once said<sup>8</sup> "He (Marx) discovered the simple fact that human beings must have food and drink, clothing and shelter, first of all, before they can interest themselves in politics, science, art, religion, and the like." The satisfaction of these and other wants for economic goods requires productive activity, and the time has long since passed when production can be successfully carried on as an individual process. Almost universally in the capitalistic system, production is of necessity a social process which involves the cooperative activity of considerable numbers of individuals. Thus, in order to satisfy their economic wants, men enter into productive relationships with each other. These relationships are independent of the will of the individual and correspond to a definite stage of development of the material forces of production. Thus, if a man wants to be a steel worker today he will have to fit himself into one of the various functions or categories of work which exist in the steel industry as it is now carried on. A choice of jobs he may have, but he cannot lay out a job for himself without

<sup>7</sup> Karl Marx, *A Contribution to the Critique of Political Economy*, (1859) Chicago Charles H. Kerr & Co., 1913, pp. 11-12.

<sup>8</sup> In an address at the funeral of Marx, March 17, 1883.

regard for the functions and tasks of other workers. The present relations of production are beyond his volition. Moreover, the relations of production in any given field or industry change greatly through time. A worker entering the steel industry today would find an existing set of productive relationships which differs sharply from those which prevailed in the same industry some fifty or a hundred years ago. However, at any particular time, these productive relationships depend upon the existing stage of development of the material forces of production.

The sum total of the productive relationships in all fields of productive activity constitute the economic structure of society or mode of production, and all other institutions and processes of human life are adapted to this mode of production. When the mode of production changes, other changes must occur sooner or later in legal relationships, government and political institutions, social institutions, religion, art, and even the mental processes of people. The tribal organization of government with a chief at the head would be completely inconsistent with the modern capitalistic mode of production and could not exist along with it. Much the same thing would be true of the ancient organization of the family, called polyandry, in which one wife had several legal husbands. In all cases, the other social institutions and processes must be adjusted to the changing mode of production. Much the same thing is true of human thought, ideas, and mental processes. It would have been almost impossible for the classical economists of the late eighteenth and early nineteenth centuries to have written treatises on economics which closely resembled those of the earlier Mercantilists which were written when feudal barriers to trade had been breaking down, inter-regional and international trade had been developing, and the merchant-traders had been the relatively scarce or insufficient class in the population. Mental attitudes toward practically all matters change along with the changing mode of production.

The mode of production which is to have such miraculous and far-reaching influences cannot be interpreted narrowly to mean merely the existing technology of production—tools and machinery—for it would be ridiculous to think that all social institutions and processes derived their entire form and content from such a narrow base. The mode of production includes the existing technology of production, but there is ample evidence in the writings of Marx and his followers that it includes a great deal more as well. Appar-

ently the mode of production must take account of the number of available workers, their characteristics and abilities, their productiveness, their organization, and their cooperation or the extent to which the division of labor is practiced. It includes the quantity and quality of land available, the abundance or shortage of mineral and other natural resources or types of power, and other natural things. It includes, according to some interpreters, the extent to which transportation and communication have been developed, and even the institutions and processes which have been developed for the exchange of economic goods, as distinguished from their production in the narrower sense. Truly the mode of production must be closely identified with the entire existing stage of economic development.

The changes in other social institutions and processes which result from changes in the mode of production may have to do with matters of form and organization rather than basic character and substance. For example, according to Marx, the changing mode of production does nothing to change the basic character of the state, which is always an agency of oppression. The concept of the state has to do with the public power of coercion as separated from the aggregate body of citizens. The state is to be distinguished from government, which is merely the machinery in which the power resides and through which it is wielded. The state is "the political embodiment of a certain form of class-domination, corresponding to a certain set of economic relationships, which in turn arises out of a certain stage in the development of the powers of production. Accordingly, the state is . . . not an association of citizens bound together in pursuance of a common purpose, but essentially coercive, standing for the power of the ruling class to punish all offences which threaten the established system of class relationships."<sup>9</sup> Political power exercised through government is nothing more than the organized power of one class for oppressing another.

Now the change from earlier economic systems to modern capitalism has done nothing to change the nature of the state. It has perhaps been necessary to change some of the forms and organizations of government, and certainly the control of the state has passed from other individuals or groups to the bourgeoisie, or the powerful owners of productive wealth under capitalism, but that is all. The

<sup>9</sup> G. D. H. Cole, *What Marx Really Meant*, p. 180. Reprinted by permission of Alfred A. Knopf Inc., New York.

executive of the modern state is nothing more than a committee for managing the common affairs of the bourgeoisie as a whole, and the state itself is merely the organized collective power of the possessing classes which is used against the exploited and down-trodden workers, or proletariat. The state will always remain an agency of oppression until some day when the classless society of ideal communism is reached. Then, in the absence of any class to exploit, the state will wither away and disappear.

According to the notion of modern Marxists, all arguments over differences between forms of government are ridiculous, for there is really only one form of government and that is a dictatorship in the hands of the dominant class of the time, which, under capitalism, is the bourgeoisie. The bourgeois dictatorship works very well under the so called democratic form of government. Under democracy, the possessing class wields its power indirectly but all the more effectively because in this way its control of the government is partly concealed. The owning class controls the government by means of the corruption of governmental officials and legislatures, bribery, lobbying, the direct control of votes and of the details of suffrage, and the control of newspapers, periodicals, radio, and other agencies for molding public opinion. And the owning class very cleverly obtains the support of the exploited masses. Every so often, the government goes to the trouble of holding an election, the people have a choice of candidates and platforms, and they ostensibly elect their rulers for the ensuing period. Actually, however, the opposing candidates are as nearly alike as two peas in a pod, and the elections mean merely that every few years the oppressed have a chance to decide which agents of the oppressing class shall have charge of oppressing them in the following period.

Marx's notion of the nature of the state and government, and of its strict control by the bourgeoisie, was doubtless the source of his opinion that the oppressed masses could alleviate their misery effectively only by means of revolution. The bourgeoisie might permit the government to make certain concessions to the masses by means of progressive or social legislation, but such concessions would never be carried far enough to create any real change in the existing system or to endanger the power of the dominant class. Any concessions to the masses would be intended to bolster up and perpetuate the existing system and not to tear it down. Whatever other mistakes the bourgeoisie may make, they will never commit suicide.

Neither did there appear to be anything very hopeful about the activities of labor organizations, for the government as controlled by the bourgeoisie would never permit these organizations to develop to such an extent or in such ways as would actually endanger or infringe upon the powers of the dominant class. No wonder Marx could urge the workers of the world to unite and could contend that they had nothing to lose but their chains.

*The Marxian Philosophy in Relation to the Interpretation of History.* The Marxian interpretation of history should be considered undoubtedly as an example of the use of the Marxian dialectic or method of explanation, though it would seem that the dialectic can be applied to the interpretation of history in more than one way. If, out of a past situation, a change in the mode of production has arisen, we may consider this to be a thesis which finds its negation or antithesis in the old social, political, and legal institutions, thoughts and theories, which continue to exist for a time. There is certain to be conflict or struggle between the new mode of production and the old ideas and institutions of a social, political, and legal nature, and this conflict will result sooner or later in a synthesis, or negation of the negation. The synthesis will involve a new situation in which human ideas and social, political, and legal institutions will once more be in adjustment with the mode of production. Or the old set of institutions and ideas could be considered as the thesis, which finds its antithesis in the changing mode of production, with the same final result occurring as in the other illustration. The synthesis, in which the mode of production is once more in adjustment with human ideas and social, political, and legal institutions, would then be a new thesis which would once more be disrupted by a change in the mode of production, and so on and on.

However, according to some people, another interpretation of historical events in terms of the dialectic is more meaningful. That is, we should consider the mighty bourgeoisie as the fundamental fact or thesis of capitalism which finds its contradiction or antithesis in the downtrodden masses or proletariat. The conflict between thesis and antithesis is the famous "class struggle" which Marx emphasized so strongly. The outcome is eventually the breakdown of capitalism, and the final synthesis is found in the classless society of ideal communism. This interpretation could obviously be valid once, but Marx usually regarded the dialectical process as continu-

ous, and it is difficult to see just what the negation or antithesis of the classless society, which would help to produce further change, would be. We do not know whether Marx considered the classless society to mark the end of the dialectical process in history, or whether he merely thought that changes beyond that point would occur but simply could not be anticipated.

Finally, it might be possible to find illustrations of thesis, antithesis, and synthesis within the mode of production itself. The single enterprise form of business organization as thesis might have found its antithesis in the factory system of specialized, large-scale, and roundabout production, and the conflict might be considered to have resulted in the modern corporation which is well adapted to production of the new type. However, someone would object that the single enterprise and corporation are forms of organization which are part of the legal superstructure of society rather than the economic base or mode of production. This points clearly to one difficulty of interpretation, for Marx and Engels never stated at all definitely just where the line should be drawn between the mode of production itself and the superstructure of legal, political, and social institutions.

*The Strength of the Marxian Interpretation of History.* The Marxian interpretation of history has come in for a great deal of enthusiastic acclaim and bitter criticism. On the whole, it may be considered a rather good explanation of history. Certainly it may be compared favorably with earlier interpretations which described historical events as progressive manifestations of a divine will or providence, as the products of changing human ideas and thoughts, or as the creations of a long succession of great men. With the economic basis of historical events firmly in mind, we can interpret the overrunning of western Europe by Gauls, Teutons, Huns, and Tartars in terms of drought, famine, and the lure of plunder, the Crusades as designed to protect the trade of Genoa and Venice against the Saracens and Turks, and the American revolution in terms of unpopular taxation and immigration laws. Historical events usually do have some kind of an economic basis, and this fact was not thoroughly recognized before Marx's time.

While we cannot estimate the extent to which the development can be attributed to the work of Marx and Engels, it seems rather clear that historical writings today pay much greater attention to economic factors than did those of many years ago and are no

longer merely accounts of generals, kings, and battles. No historian of modern times would attempt to explain either World War I or II without delving deeply into a variety of economic matters. Other types of social studies vie with each other also in their emphasis on economic matters. If a sociologist notes that the social institution known as the family is not today what it was a hundred years ago and attempts an explanation, he is likely to mention such things as changing methods of production which make it possible for women to enter many types of work which were formerly closed to them, the ability of women to support themselves economically so that they are no longer dependent upon their husbands through life for shelter and a meal ticket and therefore do not have to put up with their husbands regardless of their actions, and the urbanization of the population which has resulted in the substitution of the one and a half room apartment for the old family home with its deeper roots. In similar fashion, any political scientist who set out to explain why the government of the United States today is not what it used to be fifty or a hundred years ago and completed his discourse without referring to a multitude of economic factors and forces would be deserving of some kind of a medal. The importance of economic activities in relation to other human activities has been recognized much more clearly since Marx's time than before.

*Criticism of the Marxian Interpretation.* The most common criticism of the Marxian interpretation of history holds that, while Marx had a really good idea, he greatly overemphasized it. Historical events are extremely complex, and any attempt to account for them in terms of a single factor, whatever it may be, is sure to be deficient to a certain extent. Thus, it is held that the Marxian interpretation of history either overlooked many significant non-economic factors or attributed insufficient importance to them. One such factor is said to be the geographical environment. Climate, soil, topography, access to oceans, and the presence or absence of various natural resources play a most important part in determining occupations, modes of living, interests, the extent of geographical division of labor, and general economic development. Marx is accused of paying little attention to the economic effects of geographical factors and of overlooking their noneconomic effects almost completely.

Religion is a second important factor in human life. Marx and Engels did not overlook religion but they considered it to be derived

rather directly from the economic sub-soil. Thus, Marx said that religion is but the reflex of the real world, and Engels wrote "All religion is nothing but the phantastic reflection in men's minds of those external forces which control their daily life a reflection in which the terrestrial forces assume the form of supernatural forces."<sup>10</sup> On this basis, Engels went on to show that the ecclesiastical hierarchy of the Middle Ages was closely related to the feudal hierarchy and that the comparatively mild heresy of the Protestant Reformation resulted from the growing power of the bourgeoisie. Many people have questioned this attitude which makes religion the mere servant of an economic master. It seems to them that religion, regardless of its ultimate origin, is an important force in the lives of many people and one which has accomplished results of tremendous significance either by itself or in conjunction with a variety of economic and noneconomic factors.

It is further contended that Marx underestimated the importance of the human mind and ability to think in developing his interpretation of history. We may admit that human thought is conditioned and influenced by changes in the economic environment and that human thoughts are not likely to be of great importance unless they are related in some way to the objective facts of human existence. As Cole has suggested, men are not limited to thinking about the current problems of their age, but more will do so than not, and only those ideas which have significance for their age will influence the course of history.<sup>11</sup> On the other hand, ideas develop also from those which have been accumulated previously and do not always result directly from external facts. As a matter of fact, one group of ideas may readily give rise to another without the intervention of any changes in external circumstances.

Finally, a closely related matter is that of science and research, which Marx regarded as important but attributed to a rather completely economic origin. Many people question whether the development of science can be attributed solely to economic needs and regard it as the product of a large number of factors. Many phases of scientific research deal with matters which are not at all directly economic in character and there are many scientists and inventors who are apparently motivated by many factors besides self-interest.

<sup>10</sup> Friedrich Engels, *Anti-Duhring*, New York: International Publishers, 1934, p. 316.

<sup>11</sup> G. D. H. Cole, *What Marx Really Meant*, pp. 81-82.

or the desire for immediate economic gain Once a science has got under way, it often seems to develop on its own power without any further intervention of outside forces Moreover, the stage of economic development may furnish all the background and raw materials necessary for a certain invention or scientific development, but not everyone hits upon such a discovery In fact, many people may use the background and materials only to produce relatively inconsequential or even useless devices Serious discoveries and inventions apparently require the intervention of particular individuals with special qualities of mind And so the critics have gone on and mentioned factors which they regard as noneconomic but which have nevertheless been important in influencing the course of history

Of course, a good Marxist might object that many of these criticisms are beside the point, because the mode of production, as broadly defined, includes many of the factors which Marx is accused of overlooking or underestimating Thus, as we have seen, the mode of production is frequently taken to include all geographical factors (such as soil, climate, topography, natural resources, and sources of power), and perhaps science and invention as well It is also contended that Marx attached much greater significance to the workings of the human mind than the critics seem to think However, this opens the way to another type of criticism If Marx had "discovered" that the mode of production, in the narrow sense of technology or tools and machinery, was the sole determinant of history and cause of change in political, social, and legal institutions and human ideas, it would have been a wonderful discovery except for the fact that it obviously is not true On the other hand, as the mode of production is broadened so that it comes to include more and more factors, the chance that it can function as specified in the Marxian interpretation increases, but the significance of Marx's discovery decreases There is apparently no limit on the process of bringing more factors into the mode of production until the point is reached where the mode of production contains everything Then the Marxian interpretation of history merely says that "everything determines everything"—a proposition which is obviously true and one which, equally obviously, is meaningless as an interpretation of history

*Qualifications of the Marxian Interpretation of History* To some extent, the criticism of the Marxian interpretation of history has re-

sulted from a misunderstanding of its meaning It would be absurd to contend that, when the mode of production changes, we must expect to see our legal, political, and social institutions and habits of thought also change overnight as it were, but this is not what Marx contended In his opinion, the effects of changes in the mode of production on various institutions and habits of thought need not be direct, immediate, or even perceptible to the people Instead, these effects may work themselves out slowly, gradually, and unconsciously The Industrial Revolution occurs and several decades later we suddenly discover that the government, the family, and our thoughts on economic and other matters are not what they used to be Obviously, there is something in this situation which is similar to the "cultural lag" which some sociologists have emphasized This introduction of the time-lag concept makes the Marxian interpretation of history seem much more reasonable than it would otherwise, but it also lessens the chance to verify or disprove its validity

Other qualifications of the Marxian interpretation of history ascribe some history-making powers to other noneconomic factors, at least in a secondary way That is, once the changing mode of production has had its effect on social, political, and legal institutions and on habits of thought, these factors may in turn act on each other and on the mode of production in influencing the course of history This qualification may seem to weaken the strict Marxian interpretation of history but it is often made Even Engels once said,

According to the materialist conception of history the determining element in history is ultimately the production and reproduction in real life More than this neither Marx nor I have ever asserted If therefore somebody twists this into the statement that the economic element is the only determining one, he transforms it into a meaningless, abstract, and absurd phrase The economic situation is the basis but the various elements of the superstructure—political forms of the class struggle and its consequences, constitutions established by the victorious class after a successful battle, etc—forms of law—and then even the reflexes of all these actual struggles in the brains of the combatants political, legal, philosophical theories, religious ideas and their further development into systems of dogma—also exercise their influence upon the course of the historical struggles and in many cases preponderate in determining their form There is an interaction of all these elements, in which, amid all the endless host of accidents (i.e., of things and events whose inner connection is so remote or so impossible to prove that we regard it as

absent and can neglect it), the economic movement finally asserts itself as necessary. Otherwise the application of the theory to any period of history one chose would be easier than the solution of a simple equation of the first degree.<sup>12</sup>

And again

Political, juridical, philosophical, religious, literary, artistic, etc., development is based on economic development. But all these react upon one another and also upon the economic base. It is not that the economic position is the *cause and alone active*, while everything else has only a passive effect. There is, rather, interaction on the basis of the economic necessity, which *ultimately* always asserts itself. Men make their history themselves, only in given surroundings which condition it and on the basis of actual relations already existing, among which the economic relations, however much they may be influenced by the other political and ideological ones, are still ultimately the decisive ones, forming the red thread which runs through them and alone leads to understanding.<sup>13</sup>

Further

Marx and I are ourselves partly to blame for the fact that younger writers sometimes lay more stress on the economic side than is due to it. We had to emphasise this main principle in opposition to our adversaries, who denied it, and we had not always the time, the place or the opportunity to allow the other elements involved in the interaction to come into their rights.<sup>14</sup>

In the end, the most meaningful and reasonable version of the Marxian interpretation of history, though it is somewhat weaker than the original Marxian version, seems to be that advanced by Cole. He says

Men make their own history but they can make it in any constructive sense, only by accepting the limitations and opportunities of the age in which they live. What can be argued is that however men decide to act the economic forces will in the long run make their action ineffective unless it is in sufficient harmony with the requirements of the economic situation. The economic conditions circumscribe, but by no means abrogate, human freedom and in a given situation there may be many

<sup>12</sup> Marx Engels *Selected Correspondence* New York International Publishers 1935, p. 175 (Engels to J. Bloch) Reprinted by permission of the publishers

<sup>13</sup> *Ibid.*, pp. 517-518, (Engels to H. Sturkenburg) Reprinted by permission of the publishers

<sup>14</sup> *Ibid.*, p. 177 (Engels to J. Bloch) Reprinted by permission of the publishers

alternative courses open, none of which is impossible on economic grounds. Within this wide range of choices the non-economic forces are free to operate inducing men to do this in preference to that on what ever grounds may appeal to them and thus vitally influencing the movement of historical events. Only when men try to pass beyond the limits set by the absolute possibilities of the economic situation are they sharply pulled back into a path consistent with the requirements of economic development.<sup>1</sup>

### *The Class Struggle*

The Marxian interpretation of history, or doctrine of historical materialism, is merely a prelude to, and a general foundation for, the development of the more special doctrine of the class struggle, which is to result, according to Marx, in the destruction of capitalism and the eventual establishment of the classless society. Class struggles are nothing new, for they have existed in all times and places and have been a most potent source of historical development. As Marx and Engels said:

The history of all hitherto existing society is the history of class struggles. Freeman and slave, patrician and plebeian, lord and serf, guild master and journeyman in word, oppressor and oppressed, stood in constant opposition to one another, carried on an uninterrupted, now hidden, now open fight a fight that each time ended either in a revolutionary reconstitution of society at large, or in the common ruin of the contending classes.<sup>2</sup>

However, while class struggles have always existed, the class struggle under capitalism is more open and clear cut than those of earlier times.

In the earlier epochs of history, we find almost everywhere a complicated arrangement of society into various orders, a manifold gradation of social rank. In Ancient Rome we have patricians, knights, plebeians, slaves, in the Middle Ages, feudal lords, vassals, guildmasters, journeymen, apprentices, serfs, in almost all of these classes, again, subordinate gradations. The modern bourgeois society that has sprouted from the ruins of feudal society has not done away with class antagonisms. It has but established new classes, new conditions of oppression, new forms of

<sup>1</sup> G D H Cole, *What Marx Really Meant*, pp 90-93 Reprinted by permission of Alfred A Knopf, Inc., New York

<sup>2</sup> *The Communist Manifesto* Chicago Charles H Kerr & Company 1915, p 12

struggle in place of the old ones Our epoch, the epoch of the bourgeoisie, possesses, however, this distinctive feature, it has simplified the class antagonisms Society as a whole is more and more splitting up into two great hostile camps, into two great classes directly facing each other—Bourgeoisie and Proletariat<sup>17</sup>

*The Nature of the Classes* The distinguishing characteristic of the bourgeoisie is the ownership of property—property in money funds or more especially in land and capital instruments Since all members of the bourgeoisie live on income derived from the exploitation of the proletariat, Marx makes no strong distinction between money-lenders, land owners, and capitalist-employers but lumps them all together in the bourgeoisie The proletariat, on the other hand, consists of the great masses of wage earners, who have no property in productive wealth or surplus money funds and who must therefore live by selling their labor, or labor-power, to the bourgeoisie in return for wages which are in turn exhausted in providing for the maintenance and reproduction of the workers Marx did not contend that capitalistic society was already completely divided into these two groups, for he recognized a middle class or petty bourgeoisie which fell in between the two main groups This petty bourgeoisie included small manufacturers, shopkeepers, artisans, and peasants, all of whom were conservative, if not actually reactionary, in their economic attitudes It also presumably included the professional groups, although Marx once apparently consigned them to the proletariat by asserting that the bourgeoisie had converted doctors, lawyers, priests, poets, and scientists into its paid wage-laborers

The existence of a middle-class group did not worry Marx and Engels, because it seemed to them that this group was on its way out As the *Communist Manifesto* said

The lower strata of the Middle class—the small tradespeople, shop keepers, and retired tradesmen generally, the handicraftsmen and peasants—all these sink gradually into the proletariat, partly because their diminutive capital does not suffice for the scale on which Modern Industry is carried on, and is swamped in competition with the large capitalists, partly because their specialized skill is rendered worthless by new methods of production<sup>18</sup>

<sup>17</sup> *Ibid.*, pp. 12-13

<sup>18</sup> *Ibid.*, p. 23

The proletariat is also enlarged from time to time by persons who desert the higher groups on their own volition

A small section of the ruling class cuts itself adrift and joins the revolutionary class, the class that holds the future in its hands. Just as, therefore, at an earlier period, a section of the nobility went over to the bourgeoisie, so now a portion of the bourgeoisie goes over to the proletariat, and in particular, a portion of the bourgeois ideologists, who have raised themselves to the level of comprehending theoretically the historical movements as a whole<sup>19</sup>

It is worthy of note that, while Marx made ample provision for other persons of higher rank to sink into the proletariat, he apparently considered it impossible for members of the proletariat to rise to positions in the middle class or the bourgeoisie

*The Development of the Class Struggle* The modern capitalistic class struggle began with the breakdown of conditions existing in the old feudal society. In the so-called period of primitive accumulation of capital, some persons acquired the productive wealth and money funds which enabled them to hire and exploit labor, while others did not

The spoliation of the church's property, the fraudulent alienation of the State domains, the robbery of the common lands, the usurpation of feudal and clan property, and its transformation into modern private property under circumstances of reckless terrorism were just so many idyllic methods of primitive accumulation. They conquered the field for capitalistic agriculture, made the soil part and parcel of capital, and created for the town industries the necessary supply of a 'free' and outlawed proletariat<sup>20</sup>

Since the period of primitive accumulation, the members of the bourgeoisie have lived on income derived from exploiting the labor of the toiling masses, or proletariat. This income not only affords the members of the bourgeoisie a good living but also permits the further accumulation of capital for still greater exploitation of the proletariat. The members of the latter group, since they are propertyless, must sell their labor-power for a price or wage which is only sufficient for their subsistence and reproduction. Thus the rich get richer in relation to the poor and the clash of interests between

<sup>19</sup> *Ibid.*, p. 26

<sup>20</sup> Karl Marx, *Capital*, Volume I, p. 805

bourgeoisie and proletariat is harsh and irreconcilable Nothing would completely satisfy the members of the proletariat except the receipt of the full value of the products created by their labor, and this result (though entirely impossible under capitalism) would result in the elimination of the bourgeoisie through the destruction of their only source of income Hence, we may expect nothing except a struggle to the death between these opposing groups

Marx and Engels, in the *Communist Manifesto*, relate a long list of accomplishments in the past which may be attributed to the activities of the bourgeoisie

The bourgeoisie has been the first to show what man's activity can bring about It has accomplished wonders far surpassing Egyptian pyramids, Roman aqueducts, and Gothic cathedrals, it has conducted expeditions that put in the shade all former Exodus of nations and crusades The bourgeoisie, during its rule of scarce one hundred years, has created more massive and more colossal productive forces than have all preceding generations together Subjection of nature's forces to man, machinery, application of chemistry to industry and agriculture, steam-navigation, railways, electric telegraphs, clearing of whole continents for cultivation, canalization of rivers, whole populations conjured out of the ground—what earlier century had even a presentiment that such productive forces slumbered in the lap of social labor<sup>21</sup>

However, from the point of view of the entire history of capitalism, the most significant accomplishment of the bourgeoisie is found in the creation, establishment, and development of the proletariat, whose members will one day function as grave-diggers for the bourgeoisie

And the bourgeoisie deserves to perish because as Marx and Engels say

The bourgeoisie, historically, has played a most revolutionary part The bourgeoisie, wherever it has got the upper hand, has put an end to all feudal, patriarchal, idyllic relations It has pitilessly torn asunder the motley feudal ties that bound man to his "natural superiors," and has left remaining no other nexus between man and man than naked self-interest, than callous "cash payment" It has drowned the most heavenly ecstasies of religious fervor, of chivalrous enthusiasm, of philistine sentimentalism, in the icy water of egotistical calculation It has resolved personal worth into exchange value, and in place of the numberless indefeasible chartered freedoms, has set up that single, unconscionable

<sup>21</sup> *Communist Manifesto*, pp. 16, 18, and 19

freedom—like Trade. In one word, for exploitation, veiled by religious and political illusions it has substituted, naked, shameless, direct, brutal exploitation.

*The Interpretation of Ancient Class Struggles.* We must wait until a bit later on to examine the exact details of the process by means of which the capitalistic system is to be brought to its doom and the class struggle is to be replaced by the classless society. However, at present, we may direct several criticisms at the Marxian analysis of the class struggle itself and of the participating groups. In the first place, the Marxian claim that the "history of all hitherto existing society is the history of class struggles" seems to be refined, according to the critics by general history with which Marx was inadequately acquainted. To select one ancient example out of the several cited by the critics:

Ancient civilizations such as those of Egypt, Greece, and Rome, were based on the institution of slavery, whence the gratuitous assumption of Marx and Engels that the class struggle must have dominated their historical development and finally brought about the transition to the next stage of feudalism. But the slaves of those days were for the most part subservient objects, and helpless creatures, whose occasional mutinings and rebellions were suppressed with horrible cruelty. Those were not class struggles of the imaginary Marxian type, and did not bring the transition to feudalism. Engels himself says that toward the end of the Roman Empire slaves were scarce and dear, that the latifundia, which were great agricultural estates based on slave labor were no longer profitable, that small-scale farming by colonists and tenants was relatively lucrative, and that, in short "slavery died because it did not pay any longer." Then came the barbarian invasion, the downfall of Rome, and the establishment of feudalism is the result of the conquest of a higher civilization by a lower and not through the alleged driving force of a class struggle.<sup>22</sup>

*Difficulties in Distinguishing Classes.* The concept of the class struggle presupposes the division of society into two large groups or hostile camps, but it is very difficult to distinguish any such groups in the United States today. If we followed the Marxian definitions strictly, the result would be ludicrous for the purposes of socialism. That is, if we tried to divide the people of this country

<sup>22</sup> *Ibid.*, p. 15.

<sup>23</sup> J. F. LeRouge, *From Marx to Stalin*, pp. 152-153. Reprinted by permission of the Thomas Y. Crowell Company, New York.

into two groups on the basis of whether they owned or did not own property in productive wealth or money funds, we should have to place most of the people in the owning group or bourgeoisie. The only people whom we could place in the proletariat would be those who owned no land or capital directly, who had no savings deposits, who had no social security accounts to provide them with annuities in their old age, who had no life insurance policies, and who owned no corporate securities or government bonds, for all of these things involve, directly or indirectly, the ownership of productive wealth, or of money funds beyond immediate needs in consumption. A class division which results in only a few people being left in the proletariat is anything but that which Marx and Engels had in mind, and it would be difficult to see any mortal class struggle going on between such groups. Moreover, the groups would cut across each other to a considerable extent. Some individuals may readily receive \$10,000 a year from the sale of their labor services only, while others live on incomes of \$2000 or \$2500 which are derived from the ownership of property. It would seem very peculiar in any case to class the former individuals as members of the proletariat and the latter individuals as members of the bourgeoisie.

Many modern Marxians realize that the original definitions of the parties to the class struggle are in need of revision for application to capitalism of the present day. Sometimes it is suggested that we should include in the proletariat not only persons with merely labor incomes but also persons with some property incomes as well, just so long as the property incomes are less important than the labor incomes. In the bourgeoisie, we should have all persons with only property incomes and those whose property incomes exceeded their labor incomes. Now it would obviously be possible to divide society into two groups on this basis, but it is to be doubted that they would be highly antagonistic and conflicting groups. Surely a person who derives 49 per cent of his income from the ownership of property is going to have about the same economic interests and attitudes as one who derives 51 per cent of his income from this source, and one would have to go rather well down into the so-called proletariat before finding any real change in these interests and attitudes.

It might be well to remember, in trying to distinguish two conflicting groups in our society today, that the control of productive wealth is usually more important than its ownership. Thus, we

could divide society into two groups according to whether individuals did or did not control significant amounts of productive wealth. While there would obviously be difficulties in applying this notion in practice, we should expect to come out with a relatively small number of powerful individuals in the bourgeoisie and with a proletariat made up of a large number of persons who are powerless so far as the *control* of productive wealth is concerned. There can be no doubt as to the existence of a conflict of interests between the two groups set up in this way, but whether this conflict is as yet open and bitter enough to satisfy the Marxian concept, it is difficult to say.

Many people think, however, that it is useless to try to see our society as divided into two groups, with the one above the other. Actually, there are many economic groups, and they divide the society into horizontal segments or sections rather than into layers. The interests of such economic groups as, for example, farmers, manufacturers, and workers are in part conflicting and antagonistic and in part common and harmonious. The groups have undoubtedly a certain amount of class or group consciousness, but it is not usually of the type which makes cooperation or compromise with other groups impossible. If this is an accurate description of our social situation, it is clear that our society departs significantly from the Marxian formula.

*The Survival of the Middle Class* Getting back to the Marxian description again, it is rather clear that the middle-class group or small bourgeoisie has not disappeared in this country, either by the dismal process of sinking back into the propertyless proletariat or otherwise. Several studies might be quoted which indicate that the group of persons who are neither extremely prosperous nor exceptionally poor has been increasing through time in numbers, wealth, income, and as a proportion of the total population. On this basis, some observers are led to think rather enthusiastically that the polarization, which Marx had expected to occur at the extremes of capitalistic society, has actually taken place in the middle. Such studies and conclusions depend, however, on rather arbitrary decisions as to the boundaries of the middle class group in terms of income.

Perhaps even more important than the *existence* of groups or classes is the matter of class *attitudes*. It matters rather little that we may have groups which might be described as bourgeoisie and

proletariat on the basis of income status or general economic position unless these groups are properly class-conscious. If all members of the population, regardless of their income status, think like members of the middle class, then for almost all practical purposes bourgeoisie and proletariat do not exist. And this seems to be just about the case in the capitalistic system of the United States today. Canvasses and polls taken on this important subject, which have questioned people in all walks of life and at all sorts of income levels, have usually discovered that somewhere between 80 and 100 per cent of our citizens consider themselves to be members of the "middle class" rather than members of the exceptionally prosperous or extremely poor and underprivileged.

Evidence of this attitude can be found in the activities of large groups of wage-earners in the United States. If certain workers are dependent on their labor incomes for their entire livelihood and they find these labor incomes unsatisfactory, they do not usually blame the capitalistic system and set about forming organizations and carrying on activities for the purpose of destroying this system. Instead, they try to improve their economic position within the capitalistic system by forming organizations for bargaining purposes, restricting output as the employers do, forming quasi-monopolies over the labor supplies on which employers are dependent, and in general seeking to divert a larger share of the available social income to themselves. Workers who think and act in such ways can scarcely be considered to be members of the proletariat, in the Marxian sense of the term, even though they are propertyless and dependent upon the sale of their labor power. As an English communist writes:

There is a fundamental unreality in the attitude and policy of labour today. It accepts the old system and onto the old system seeks to fasten parasitically high wages, social services and unemployment insurance.

Labour in its consciousness is capitalistic, to be parasitic on capitalism is to be capitalistic. Labour has forgotten how to be radical.<sup>24</sup>

*The New Class Struggle.* As a result of these considerations, many people conclude that the class struggle in the Marxian sense is a myth in so far as the United States of today is concerned. However concern is sometimes expressed over a new kind of class struggle.

<sup>24</sup> J. M. MUIR, *The Necessity of Communism* London: Jonathan Cape, 1932 pp. 78-104.

which is or may be developing. As our total population becomes first stationary and later actually declining, an ever larger proportion of our people will be found in the advanced age groups. These superannuated persons cannot be expected to take an active part in the productive activities of the country and will rely on the actually productive portion of the population for support. Unless one believes in the Townsend theorems, it seems rather obvious that we can devote a larger share of the national income to the support of the aged only by leaving a smaller portion of this total income in the hands of those who take an active part in the processes of production. Thus, there will be a clash of interests as between the aged group and the rest of the population, and this clash may result in an actual class struggle in which each group attempts to control the national government in its own interests and tries to gain a larger share of the national income for itself. For the present, however, this struggle, if it exists, is no more than in its opening phases, and its exact future development cannot be accurately foretold.

#### QUESTIONS

- 1 What were the main principles of Hegelian philosophy?
- 2 To what extent did Marx adopt the Hegelian philosophy in his writings? What modifications did he make in this philosophy for his purposes?
- 3 Why did Marx try to develop an interpretation of history? Explain
- 4 Outline the Marxian interpretation of history
- 5 Explain the meaning and importance of the term "mode of production" as used by Marx in his interpretation of history
- 6 "The Marxian interpretation of history may be considered as an application of the Marxian dialectic (involving thesis, antithesis, and synthesis)." Explain and illustrate
- 7 Evaluate the Marxian interpretation of history, stressing points of both strength and weakness
- 8 "There are no sound objections or criticisms which may be directed at the Marxian interpretation of history." Show whether you agree
- 9 "The Marxian interpretation of history either overlooked many significant noneconomic factors or attributed insufficient importance to them." Do you agree? Explain
- 10 "The Marxian interpretation of history explains either too much or too little." Discuss
- 11 How has the Marxian interpretation of history been qualified by Engels and others?

- 12 "The most meaningful and reasonable version of the Marxian interpretation of history seems to be that advanced by Cole" Explain
- 13 "According to Marx, the state is always an agency of oppression and all forms or types of government are dictatorships in reality" Explain
- 14 What is the importance of the class struggle according to Marx?
- 15 Distinguish between the bourgeoisie and the proletariat as Marx described them
- 16 What was to be the outcome of the class struggle, according to Marx?
- 17 "It is difficult to distinguish the Marxian economic classes in the economy of the United States today" Show whether you agree
- 18 "It is possible that other types of class struggles are becoming more important today than that which Marx emphasized" Explain

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## CHAPTER 27

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### THE MARXIAN THEORIES OF VALUE AND DISTRIBUTION

We have noted Marx's contention that the income of the bourgeoisie under capitalism is derived from the exploitation of the toiling masses of labor, but we are not yet familiar with the manner in which this exploitation occurs. Before we can understand Marx's exploitation thesis, we must examine the Marxian theories of value and distribution on which the doctrine of exploitation is based. Many critics of Marx have contended that his theories of value and wages, like his interpretation of history, were directed primarily at changing the capitalistic system rather than at explaining its present functioning, but, ostensibly at least, he was trying to produce a valid and objective explanation of economic phenomena and their causal relationships as they existed in the period of his observation. It will be helpful to remember that Marx's explanations of value and distribution, whatever his ultimate purpose may have been, were intended to apply to the capitalistic system as it existed in his day, and not to some ideal system which he was proposing to establish.

#### *Exposition of the Marxian Theory of Value*

**Use-Value, Exchange-Value, and Price** Marx proceeded like most economists to preface his discussion of value determination with the definition of a number of terms and concepts. In the first place, he distinguished between two kinds of value which a commodity may have—use-value and exchange-value. By use-value, Marx meant the value or usefulness of a commodity to its owner, its utility (as we should say now), or the amount of satisfaction or pleasure which a user derives from the commodity. Exchange-value, on the other

hand, was the power of a commodity or economic good to command other economic goods in exchange for itself After the brief introductory reference to use-value, Marx concerned himself, like most economists, with the explanation of exchange-value The price of an economic good was defined as its power to command money in exchange for itself or as the "money-name" of the value of an economic good

Marx also gave the explanation which was common in his day of the relationship between use-value and exchange-value Clearly, an article must have use-value in order to have exchange-value, for no one will give up a commodity or service in exchange in order to get something which is expected to have no use for him On the other hand, it is quite possible for an article to have use-value without having exchange-value Such articles are commonly known in economics as free goods However, in a developing capitalistic economy, free goods tend to disappear and practically everything that has use-value also has exchange-value In all these definitions and discussions of their interrelations, there is nothing at all revolutionary or out of the ordinary

*Market Value and Normal Value* Like other economists, Marx saw fit to distinguish between the market exchange-value of a commodity and its natural or real exchange-value By natural value, Marx meant something very much like the "normal value" of our present value discussions—a kind of long-run average level of the value of a commodity around which short-run or market values fluctuate Marx thought it necessary to explain both normal values and the market values which oscillate around them It was at this point that he began to get into difficulties, for, while he was willing to concede that demand and supply forces were responsible for the fluctuations of market values around natural or normal values, he could not believe that the same demand and supply forces could be responsible for the natural or normal values themselves Thus, he said

At the moment when supply and demand equilibrate each other, and therefore cease to act, the market price of a commodity coincides with its real value, with the standard price round which its market prices oscillate In inquiring into the nature of that [real or natural] value, we have therefore nothing at all to do with the temporary effects on market prices of supply and demand<sup>1</sup>

<sup>1</sup> Karl Marx, *Value, Price, and Profit* Chicago Charles H Kerr & Company 1913, pp 45-46

The task which Marx set himself was, then, the discovery and analysis of the one factor which determines the real or natural value of all commodities. Unfortunately, the objective of Marx's work predetermined the value of his results. Most economic phenomena are extremely complex, and it is very seldom that any phenomenon can be assigned to a single cause. To try to find the one cause of the natural values of commodities is much the same as to try to find the sole and single cause of business cycles or the one and only meaning of the term "inflation." The point is not that one cannot make out a case for a particular factor, but rather that such a case is practically certain to be inadequate.

*The Rejection of Utility and Demand.* Marx could have made a great stride forward in value theory by hitting upon utility, and demand based upon utility, as a factor in determining the natural values of commodities. However, it was his notion that the value-determining factor not only had to be common to all commodities, but had to be objective and absolute (unchanging) as well, and this led him to reject use-value or utility as a subjective and relative concept. The utility of a commodity is not something physical and objective comparable to its size, shape, and weight. It is not something which is actually in the good. Utility is rather a relationship between men and things—a relationship which is expressed by saying that the men want the things. It is therefore a matter of the human mind as well as of the commodity and is a subjective concept. Since this is true, utility is also a relative concept, for the utility of the same good may be quite different for different persons, and it may be quite different for the same person from one time to another. The utility of a textbook for a student may be quite different from its utility to some unsuspecting wayfarer who picks it up after the student has lost it on his way home from class. Again, the utility of a textbook for a student who has completed the course in which it is used may be quite different from the utility which it had for him at the beginning of the course. Marx could see no use which could be made of such a subjective and fluctuating thing as use-value or utility beyond saying that a commodity must have use-value in order to have exchange-value. Certainly, so he thought, utility could not be made the basis for the relatively stable natural values of commodities. The quantitative analysis of utility and demand had not been developed up to Marx's time and he was

quite unable to develop it That task was left for another generation of economists

**The Acceptance of Labor as Value-Determining** In considering the more objective qualities of commodities, Marx was compelled to reject such things as size, color, shape, and weight, for these characteristics are important only in so far as they affect the usefulness of the commodities Therefore, by a process of elimination, Marx hit upon labor, or muscular and mental human effort, as the one objective, value-determining element common to all commodities which have exchange-value But the value-determining element had to be quantitative as well as objective, so the explanation could not depend upon the quality or type of labor used to produce a commodity So Marx fell back upon the quantity of labor, or the amount of labor-time required to produce a commodity, as the determinant of its natural value In Marx's own words

✓ A use-value, or useful article, therefore has value only because human labour in the abstract has been embodied or materialized in it How, then, is the magnitude of this value to be measured? Plainly, by the quantity of the value creating substance, the labour, contained in the article The quantity of labour, however, is measured by its duration, and labour time in turn finds its standard in weeks, days, and hours<sup>2</sup>

And again

A commodity has *value*, because it is a crystallization of social labor The greatness of its value, or its *relative value*, depends upon the greater or less amount of that social substance contained in it, that is to say, on the relative mass of labor necessary for its production The relative values of commodities are, therefore, determined by the respective quantities or amounts of labor worked up, realized, fixed in them<sup>3</sup>

**Past and Present Labor** However, Marx was not so naive as to think that the natural value of a commodity was determined by the quantity of labor-time bestowed on it in the last stages of its production only The natural value of a loaf of bread, for example, does not depend merely on the labor-time involved in mixing the ingredients, putting the dough in tins, putting the tins in and removing them from the oven, superintending the baking process, and slicing and wrapping the product On the contrary, it includes all

<sup>2</sup> Karl Marx, *Capital*, Volume I, p. 43

<sup>3</sup> Karl Marx, *Value, Price, and Profit*, p. 57

labor of these kinds and in addition all labor devoted to planting, growing, and harvesting the wheat, grinding the wheat into flour, and producing the other ingredients. To the extent that capital goods are used in the productive process, the natural value of the final product is also influenced by the labor time involved in producing these capital instruments. The value of the loaf of bread is affected by the amount of labor time bestowed in the past on the making of dough mixers and baking ovens, the farm machinery which helped in planting, cultivating, and harvesting the wheat, and even the machinery which helped to produce the farm machinery. Of course, the value of just one loaf of bread would include only a small fraction of the total amount of labor time which had been spent in producing these durable instruments of production, for this total amount of labor-time would be spread over all the loaves of bread which they help to produce during their lifetime. However, it is clear that the natural value of any final product is determined by the entire amount of labor-time which is spent on it, either directly or indirectly, in the present or in the distant past as far back as it can be traced.

We see that the basing of natural value on the total amount of labor-time used up in producing a commodity is not quite as simple a proposition as it seemed at first glance. In fact, some people find the idea of including all past and present, direct and indirect, labor-time in the price of the final product so complicated that they judge the Marxian proposition to be hopeless. "How on earth," they ask, "could anyone ever find out all the labor-time which had played a part in turning out a final product, measure it, and include it in the price of the commodity? It won't work!" The answer to this objection is, of course, the one suggested at the beginning of this chapter. Marx is not trying to explain how natural values should be determined in an ideal economy. For such a purpose, his proposition might well be considered too complicated. But Marx is merely trying to explain how natural values are determined under existing capitalism. Thus, his proposition is that the natural values which already prevail for various products in our system have been set by the processes of the market at such levels that they take account of all labor time, past and present, direct and indirect, which has been spent in their production. No individual has to settle out all these amounts of labor-time, measure them, and include them in natural value.

**Socially Necessary Labor** But this is only the beginning of our difficulties of interpretation. An article can have only one natural value at a time, but different producers may spend varying amounts of labor-time in producing exactly the same article. For example, a pair of shoes of a certain definite type can be turned out by some producers with an expenditure of five hours of labor-time, while other producers must spend six or seven hours to turn out the same product. Which of these varying amounts of labor-time will determine the natural value of shoes of this type? In order to handle this problem, Marx introduced his concept of socially necessary labor. The term "socially necessary" in this connection does not have its common modern meaning of socially desirable. Instead it means merely the average amount of labor which is necessary to turn out a particular good.

As Marx expressed this point:

In saying that the value of a commodity is determined by the *quantity of labor* worked up or crystallized in it, we mean the *quantity of labor necessary* for its production in a given state of society, under certain social average conditions of production, with a given social average intensity, and average skill of the labor employed.\*

Thus, in our illustration from shoe production, if six hours of labor-time is the average amount required to produce a pair of these shoes among all the producers in the industry, then six hours of labor-time is the socially necessary amount and sets the natural value of a pair of the shoes. Producers who use up only five hours of labor-time in producing the same commodity nevertheless tend to receive a price based on six hours of labor-time (if the price is equal to natural value), and the same price is received by those producers who, for some reason or other, use up seven hours of actual labor-time in producing the same good.

**Production and Reproduction Costs.** Suppose, at a given time, all the shoes actually on the market had required an average of six hours of labor-time to produce, but that, for some reason, the same shoes could now be produced with a social average of five hours of labor-time. Would the natural value of the shoes now on the market be set by the average of six hours of labor-time which their production actually required, or by the average of five hours of labor-time which would be required to reproduce them? In this

\* Karl Marx, *Value, Price, and Profit*, p. 62.

situation Marx did not hesitate to say that it would be reproduction cost in terms of labor-time, rather than actual cost, which would be socially necessary and hence determining in connection with natural value. Thus, he said

✓ If the time socially necessary for the production of my commodity alters—and a given weight of cotton represents after a bad harvest, more labour than after a good one—all previously existing commodities of the same class are affected, because they are, as it were, only individuals of the species, and their value at any given time is measured by the labour socially necessary, i.e., by the labour necessary for their production under the then existing social conditions

Without in any way accepting the labor cost analysis in general, most economists even today would be willing to accept Marx's judgment with respect to the relative importance of actual costs and reproduction costs.

There is a little more to be said along this line. We have been assuming that something (perhaps a new mechanical device) has operated to reduce the average amount of labor-time required to produce a commodity throughout a particular industry. But suppose only one or two firms, out of the many in a competitive industry, have adopted the new type of machinery and have reduced the amount of labor-time required to produce a unit of the good. In this case, Marx argues that the socially necessary labor-time generally required to produce the commodity has not changed, and the firm or firms with the new technological device can profit at least for a time by selling their goods at the old natural value (if price is equal to natural value) while enjoying a cost in terms of labor time which is below the social average. As the new mechanical device is adopted by more firms, it exercises a downward pull on the socially necessary labor-time required to produce the commodity and eventually the socially necessary labor-time will become that required to produce the good with the assistance of the new device. When the socially necessary labor-time and natural value have thus fallen, any firm which keeps on producing by means of the old methods will receive a price per unit for the commodity which fails to compensate it for the labor time actually spent.

*The Problem of Grades of Labor.* Suppose that the production of a particular commodity requires the use of several hours of three

or four kinds of skilled labor in addition to generous allotments of semi-skilled and unskilled labor. How will its value be determined? In handling this problem, Marx stuck to his original contention that it is only the quantity of labor, and not its quality, which has anything to do with the natural value of a commodity.

✓ While, therefore, with reference to use-value, the labour contained in a commodity counts only qualitatively, with reference to value it counts only quantitatively, and must first be reduced to human labour pure and simple.<sup>6</sup>

Skilled labour counts only as simple labour intensified, or rather, as multiplied simple labour, a given quantity of skilled being considered equal to a greater quantity of simple labour.<sup>7</sup>

But this obviously requires some exact method of converting qualitative differences in labor into quantitative differences.

However, Marx did not go beyond the general statements already recorded. Every hour of skilled labor counted as more than one hour of unskilled labor in determining the natural value of any commodity, and, since there are a great number of degrees of labor skill, there must obviously be an equally large number of multiples, or conversion factors, for reducing skilled labor to unskilled labor units. Since commodities are produced in tremendous variety in a capitalistic system and since each commodity is likely to require a combination of the various grades of labor which differs from that needed to produce every other commodity, it seems clear that the process of valuing commodities is highly complex. At this point, therefore, many students of Marx begin to wonder how he would proceed to set up all these numerous multiples or conversion factors necessary for reducing all kinds of skilled labor to unskilled. The answer is, of course, that he does not have to do anything of the sort. If he were telling us how prices or natural values would be determined in an ideal economic system, he would have to show us rather definitely how to convert various grades of skilled labor into unskilled, and perhaps work out a large number of the necessary multiples. Actually, he is describing, so he says, how the capitalistic system works in practice, and his attitude is that the natural values of commodities, as worked out on the market, already allow for all grades of skilled labor used.

<sup>6</sup> *Ibid.*, pp. 52-53.

<sup>7</sup> *Ibid.*, p. 51.

in their production in terms of proper multiples of unskilled labor. Thus, he says

✓ Whenever, by an exchange, we equate as values our different products, by that very act, we also equate, as human labour, the different kinds of labour expended upon them.<sup>8</sup>

And again

The different proportions in which different sorts of labours are reduced to unskilled labour as their standard, are established by a social process that goes on behind the backs of the producers, and, consequently, appear to be fixed by custom.<sup>9</sup>

This notion that the differences between grades or skills of labor are really quantitative in character and that skilled labor of any sort can be readily converted into unskilled labor suggests that Marx regards hereditary differences in talents and abilities as relatively unimportant. And this is precisely his attitude, as we shall see. In speaking about the wages of different grades of labor, Marx holds that the wages of skilled laborers are higher than those of unskilled laborers only by an amount which represents the cost of training the skilled workers. In other words, wages make no allowance for any natural differences in ability between workers of various grades, and it is presumably possible to make any kind of skilled labor out of unskilled labor by applying an appropriate kind and amount of training. While there are serious difficulties implicit in these conclusions which underlie the contention that skilled labor is merely a multiple of unskilled labor, Marx goes merely on to hold that the natural value of a commodity is dependent upon the socially necessary numbers of standard time units of unskilled labor used up in its production.

*Money in Relation to Other Commodities* Marx also applied his general value analysis to commodities which are used as money. Whatever the money metal may be, its natural value depends upon the amount of socially necessary labor-time required for its production and embodied in it. When commodities are exchanged for the money metal, each unit of a commodity commands in exchange whatever amount of, for example, gold or silver can be produced with an amount of socially necessary labor-time equal to that embodied in the commodity.

<sup>8</sup> *Ibid.*, p. 85

<sup>9</sup> *Ibid.*, p. 52

The value, or in other words, the quantity of human labour contained in a ton of iron, is expressed in imagination by such a quantity of the money-commodity as contains the same amount of labour as the iron<sup>10</sup>

Marx thought that the use of money and money prices was highly significant under capitalism, for the custom of expressing values in terms of money prices serves to conceal the real stuff (labor) which determines values and to convert it into an abstraction

When they assume this money-shape, commodities strip off every trace of their natural use-value and of the particular kind of labour to which they owe their creation, in order to transform themselves into the uniform, socially recognized incarnation of homogeneous human labour<sup>11</sup>

*The Significance of Land and Capital* Since we know that the production of commodities requires the use of land and capital, as well as labor, we need to see how Marx disposed of these non-human agents of production in reaching his conclusion that the natural values of commodities are determined by their content of socially necessary labor-time. We can guess the treatment which Marx accorded to capital from our earlier discussion of past and present labor costs. Capital obviously does play a part in the process of production but not as a separate and distinct type of productive agent. Capital instruments are nothing more or less than the product of past labor; they have value only because labor has been expended on them in the past, and they affect the values of the commodities which they help to produce only as so much labor. In other words, the socially necessary labor-time expended on machines and other capital instruments is part of the socially necessary labor-time which determines the natural value of the commodities which the capital instruments help to produce.

On the other hand, land and all sorts of natural things, as such, play no part in determining the natural values of commodities. All sorts of natural things have no exchange value as long as they remain in the purely natural state. They acquire exchange value only when human labor is applied to them, and even then their value depends solely on the amount of socially necessary labor-time which is applied to them. Since natural things, untouched by human labor, have no exchange value themselves, they can play no part in determining the exchange values of final commodities.

<sup>10</sup> *Ibid*, p. 108

<sup>11</sup> *Ibid*, p. 123

even though they can be used in production Similarly, when the natural things have acquired value as the result of human labor having been applied to them, they can affect the values of final commodities only to the extent of this labor which has come to be embodied in the formerly natural objects Whatever else may be said of this treatment of land and other natural objects, it is at least consistent with the general Marxian notion that human labor is the sole cause of the normal values of commodities, and consistent also with the Marxian treatment of the varying abilities of workers in connection with wages

### *Criticism of the Marxian Theory of Value*

*The Neglect of Demand* The Marxian theory of value, as outlined above, is open to a number of serious objections from the point of view of modern economic theory One of the most serious criticisms is found in the fact that Marx greatly minimized, if he did not actually overlook, the part played by demand in determining the exchange values of commodities It is possible, of course, to quote some passages from Marx which indicate that he was not entirely unaware of the influence of demand on exchange-value, but these passages are few and far between He suggests the importance of demand, for example, when he says that the mere spending of labor-time on a commodity is not enough to give it exchange value, since it must also have use-value for someone before it can have exchange-value Another indication of the significance of demand is found in the passage in which Marx states

Lastly, suppose that every piece of linen in the market contains no more labour time than is socially necessary In spite of this, all these pieces taken as a whole, may have had superfluous labour time spent upon them If the market cannot stomach the whole quantity at the normal price, this proves that too great a portion of the total labour of the community has been expended in the form of weaving The effect is the same as if each individual weaver had expended more labour-time upon his particular product than is socially necessary<sup>12</sup>

This is the same thing as saying that producers may fail to get a price which will cover cost (labor-time) either because they have produced inefficiently (using too much labor-time) or because,

<sup>12</sup> *Ibid.*, p. 120

though producing efficiently enough, they have failed to gauge the effective demand for their particular product. And Marx also suggests, in effect, that the result of a situation in which some commodities sell for less than labor cost will tend to be a redistribution of labor (and other productive resources) among industries so that the outputs of all sorts of commodities will be better adjusted than before to the relative strength of consumer demands.

On the whole, however, Marx pays little attention to demand. There is certainly no recognition of the importance of demand in the passage in which Marx says

Commodities, therefore, in which equal quantities of labour are embodied, or which can be produced in the same time, have the same value. The value of one commodity is to the value of any other as the labour-time necessary for the production of the one is to that necessary for the production of the other. As values, all commodities are only definite masses of congealed labour-time.<sup>18</sup>

Marx's general neglect of demand was unfortunate for several reasons. In the first place even if one thinks that supply factors are more important on the whole than demand factors in determining the long-run or normal values of commodities, and desires to state the basic theory of value in terms of cost, it is unwise to disregard the influence of demand, because changes in demand may readily produce changes in cost. If, for example, the demand for American wheat should increase by 50 per cent in a given period and the industry made an attempt to adjust its productive capacity to the changed demand, the better grades of wheat land would have to be cultivated more intensively than formerly or poorer grades of land would have to be brought under cultivation, or both. The additional labor and capital used in this process, whether it was applied at the intensive margin on the better lands or on poorer grades of land than those already in use, would have a lower productivity, under given methods of production, than that of the units of labor and capital formerly in use. The result of the small marginal product of the additional labor and capital would be to lower the average product per unit of labor and capital over the whole industry, and to increase the average cost per bushel of wheat whether expressed in money or in terms of labor. In converse fashion, a decrease in the total demand for American wheat would

<sup>18</sup> *Ibid.*, p. 46.

cause a reduction in the average cost per bushel of wheat in terms of money or labor. Some of the poorer land would be withdrawn from cultivation and the less intensive cultivation of the better grades of land would involve less severe penalties than formerly from the operation of the Law of Diminishing Returns, so that average product per unit of labor and capital would increase. In industries of other types, on the other hand, an increase in industrial capacity in response to an increase in demand might well result in a reduced cost per unit of output, either in terms of money or labor.

Again, in neglecting the influence of demand in value determination, Marx lost the best opportunity of his career for applying his famous dialectic. Thesis, antithesis, and synthesis are found in nearly perfect form in the field of value determination. Thesis is found in the demand for goods based on great, growing, and indefinitely expansible human wants. This thesis finds its negation or antithesis in supply, the scarcity of finished economic goods and of the means for producing them, and the obstacles which must be overcome in order to get them produced. As a result of conflict or struggle between these forces of demand and supply, certain prices or values are set on individual economic goods, and these prices or values represent a balance or synthesis of these opposing forces. All this, of course, Marx could not see or would not admit.

Finally, the neglect of demand gave Marx a badly lopsided explanation of value. It is simply not true that the normal values of economic goods are determined by cost of production alone, whether one means money cost or labor cost. Normal values in exchange are determined by two forces—cost of production, which influences supply, and utility, which influences demand. To attribute the determination of normal values to either factor alone is like giving the upper or lower blade of scissors all the credit for cutting. But, it may be objected, how much does Marx's explanation differ from that advanced by economists today? Do not economists still say that the prices of economic goods in the long run are determined by cost of production, and cannot cost of production still be resolved into labor cost, since land rent is not considered a cost of production and since capital goods are nothing more than the product of land and labor in the past?

In reality, Marx's theory of long run or normal value differs quite a little from that which is advanced by economists today. The basic proposition today holds that the price or value of an economic

good, in the long run and under competitive conditions, is determined by both supply and demand in such a way that it tends to equal average cost of production per unit. But saying that two things tend to be of equal magnitude is quite different from saying that the one determines the other. Under competitive conditions and with enterprisers economically motivated, the operation of demand and supply forces simply cannot maintain prices which are permanently above or below cost of production. It is true enough that, other things equal, the exchange value of a commodity will rise and fall with increases or decreases in labor cost or other costs per unit of product in the long run. But it is equally true that, other things equal, the exchange value of the commodity will increase and decrease with rises and falls in the desirability of the article to the consumers. Exchange value is a function of two variables, not one. Passing now to the last question raised above, cost of production is today distinctly more than labor cost. Capital goods are admittedly the product of labor, land, and previously existing capital goods, but their cost should not be viewed simply in terms of the cost of these factors. So long as individuals would rather devote their money incomes to immediate consumption than to capital purposes and so long as a payment has to be made to induce people to invest their funds in capital uses, capital goods cannot be regarded simply as congealed labor with nothing more than a labor cost. And the elimination of payments for the use of land from the category of costs of production is by no means as common among economists today as it was formerly.

Finally, it may be asked whether Marx's theory of value determination was any worse than that of other economists of his day with respect to the treatment of demand. On this point we must concede Marx a rather clean record. Many people have performed the easy but necessary task of tracing Marx's value doctrine back to those of the earlier classical economists, who also held (upon occasion, if not exclusively) that the values of commodities depended upon the labor costs of producing them. Adam Smith, for example, wrote

Labor is the real measure of the exchangeable value of all commodities

It was not by gold or by silver, but by labor, that all the wealth of the world was originally purchased, and its value, to those who possess it, and who want to exchange it for some new productions, is precisely equal to the quantity of labor which it can enable them to purchase or

command Labor is the only universal, as well as the only accurate measure of value, or the only standard by which we can compare the values of different commodities at all times and at all places.<sup>14</sup>

And again

The proportion between the quantities of labor necessary for requiring different objects seems to be the only circumstance which can afford any rule for exchanging them for one another.<sup>15</sup>

In similar fashion another early classical economist, David Ricardo, wrote

The value of a commodity, or the quantity of any other commodity for which it will exchange, depends on the relative quantity of labor which is necessary for its production and not on the greater or less compensation which is paid for that labor.<sup>16</sup>

And again

Possessing utility commodities derive their exchangeable value from two sources from their scarcity, and from the quantity of labor required to obtain them.<sup>17</sup>

Clearly, Marx could find some basis for his theory of value in the writings of these economists. On the other hand, John Stuart Mill's *Principles of Political Economy*, with its somewhat more satisfactory treatment of value determination, appeared in 1848, several years before the publication of the first volume of Marx's *Capital*, and before Marx's death the development of the marginal utility and demand analysis was very well under way, but neither of these analyses seems to have had any effect on Marx's doctrine.

However, Marx undoubtedly had to depend to some extent on the economists who preceded him and it may be asked why we bear down so heavily on Marx for neglecting the demand analysis when none of the other economists of the late 1700's and early

<sup>14</sup> Adam Smith, *The Wealth of Nations* London Thomas Nelson and Sons, 1870, Book I, Chapter 5.

<sup>15</sup> A. C. Whitaker, *History and Criticism of the Labor Theory of Value* New York Columbia University Studies, 1901, XIX, p. 20.

<sup>16</sup> David Ricardo, *Principles of Political Economy and Taxation*, Chapter I, Section 1.

<sup>17</sup> Ibid.

1800's had done any better. The answer to this question is fairly obvious. The writings of the early classical economists are of purely historical interest today. No one urges us to accept them now as adequate and accurate analyses of the workings of our modern economic system. On the other hand, the doctrines of Marx are still more or less alive. Even today, quite a few people accept them and urge them upon the rest of us as an accurate analysis of what goes on under capitalism and as a keener and more penetrating discussion of economic affairs than has been turned out by any other economist before or since Marx's time. In the light of this situation, Marx's theory of value should be judged by the standards of modern economic theory, rather than by those of the theory of his day, and the fairly obvious shortcomings of his doctrines need to be strongly emphasized.

*The Neglect of Scarcity.* Even as a supply theory of value, Marx's theory leaves much to be desired. In the first place, his desire to trace all value to labor led to an unsatisfactory treatment of the problem of scarcity. We have seen that, according to Marx, land and natural objects in general have no value so long as they remain in the natural state untouched by human labor, and even after labor has been expended on them, they never have a value which exceeds that of the labor applied to them. These conclusions seem quite unacceptable today. It seems to us that a piece of land in the middle of a city may have a large value even though it is in the natural state and no labor has been applied to it, and that land which has been developed by labor frequently has a value which is far too great to be accounted for simply by the expenditure of labor on it. It is also obvious that a diamond in the rough which we stumble over and acquire with no more labor than that required to stoop over and pick it up may be just as valuable as a diamond which is brought up from the bowels of the earth with a tremendous expenditure of human labor. Finally, getting out of the region of natural things, it seems clear that rare paintings and books, bottles of rare wine or brandy, rare stamps and coins, and a host of other things have values which cannot be accounted for in terms of labor cost. As far as we can discover, no more labor was required to produce an old stamp which is now worth \$1000 than to produce another stamp in the same year or the next year which even today is worth no more than its face value. No more labor was probably expended on a bottle of wine which is now rare

and costly than on one of a less celebrated vintage which is worth much less on the market. No more labor was necessarily required to produce a painting which later turned out to be a masterpiece worth hundreds of thousands of dollars than to produce another painting destined to remain unhonored and unsung through the years.

Marx had great difficulty in dealing with these cases. He had, to be sure, something of an escape ready to hand in the case of the soil and other natural things. He could say that our piece of land in the natural state in the center of the city would not have its present value if much labor had not been spent on neighboring pieces of land or if people did not foresee a considerable profit in applying labor to our particular piece of land. These observations seem reasonable though they represent a broadening of Marx's original position, but even these things do not help much in accounting for the great value of land which has been worked on by human labor. Again, Marx could say that the value of the diamond which we accidentally discover is not determined by the small labor cost of appropriating it but by the average cost of producing diamonds of the same size and quality, most of which have to be produced with a great expenditure of effort or labor.

It is much more difficult to account for the value of rare books, paintings, stamps, coins, and other articles which we have mentioned, in strictly Marxian terms. It is sometimes suggested that, since value is supposed to depend upon the average amount of labor-time required to produce a particular good, the value of a rare painting should not be accounted for solely in terms of the amount of labor-time spent on it. Rather we should consider the great labors of all those individuals who tried to produce masterpieces but failed. The average labor-time required to paint a masterpiece would then be far greater than the time actually spent on one. Another suggestion is that we must count all the labor-time used up in storing, caring for, and protecting the rare books, paintings, and other articles, as well as that involved in their original production. Finally, since Marx emphasized reproduction cost, some people say that the great values of these rare objects is attributable to the fact that tremendous amounts of labor might be required to turn out new objects suitable to take their place. We might keep large numbers of people working for long periods of time without producing a single masterpiece of art or literature.

or a single rare stamp or coin None of these interpretations seem entirely satisfactory, however

Actually, it is rather easy to escape from the Marxian difficulties in this matter If we do not wish to go into matters of utility and demand, we need only say that, from the point of view of supply, articles have exchange value because they are scarce Some articles are scarce because, while they are reproducible, a considerable expenditure of labor (and other productive factors) is necessary in order to produce them On the other hand, other articles are scarce because they are not reproducible at will In the latter class would fall land, diamonds, and all such things as rare paintings, books, stamps, coins, and many other items Marx, of course, was unwilling to make this explanation because it attributes the value of some things to a non-labor source However, his position is indefensible even in the light of the economics of his day, since Ricardo had clearly stated that only the value of reproducible goods was based on labor costs, while that of nonreproducible goods was based on their scarcity, it being granted that both types of articles had use-value or utility

In order to maintain his labor-cost doctrine, Marx got himself into many peculiar positions with respect to natural resources and various rare objects On several occasions, he denied that all these things are commodities, even though they are bought and sold on the market and have quite normal exchange relationships with "true" commodities He also suggested that some of these things have prices but do not have values since they are not the results of the expenditure of labor-time He said, for example

The waterfall, like the earth in general, and like any natural force, has no value, because it does not represent any materialized labor, and therefore it really has no price, which is normally but the expression of value in money Where there is no value, it is obvious that it cannot be expressed in money The price is merely capitalized rent<sup>18</sup>

On another occasion, he said

Objects that are in themselves no commodities, such as conscience, honor, etc., are capable of being offered for sale by their holders, and of thus acquiring, through their price, the form of commodities Hence an object may have a price without having value The price in that case is imaginary, like certain quantities in mathematics<sup>19</sup>

<sup>18</sup> Karl Marx, *Capital*, Volume III, p 759

<sup>19</sup> Karl Marx, *Capital*, Volume I, p 115

All such unsatisfactory dodges are the simple result of Marx's unwillingness or inability to understand that other factors besides labor-time may influence the exchange values of economic goods. *The Treatment of Capital Costs.* We have already seen that Marx did not overlook the part which actual capital instruments play in production though he thought they influenced the values of final commodities only as so much labor. In other words, capital instruments are merely past labor congealed or solidified so that it can be used in the present. Now if we always consider capital goods as already existing and disregard their fundamental source or origin, this approach may not be so bad. If we think people are just as willing to put their money incomes into capital goods as into consumers' goods, we can interpret capital goods solely in terms of the labor or other costs of producing them. However in actual practice, most people prefer to spend their money incomes for immediate consumption, regard saving and the postponement of consumption as a process which involves cost or sacrifice and will save and invest a portion of their money income only if they can obtain a reward or premium known as interest for so doing. Under such conditions, it would seem that interest should be regarded as a cost of turning out goods whose production requires the use of capital instruments and as a factor influencing the value of such final goods.

Marx knew, of course, that interest was paid for the use of capital funds in the capitalistic system of his day, but his argument seems to be that interest should not be paid and should not be a cost of production. He said that the capitalist-employers or bourgeoisie obtained their original capital by force and expropriation and that their modern sayings are just as bad. Since the workers as we shall see, tend to get only a subsistence wage, they can do no saving, and the capitalist-employers do their saving out of the surplus value or unearned income which they steal, in effect, from the workers. The capitalist-employers should get no credit and should receive no interest for savings which come out of money incomes which resulted in the first place from the exploitation of the workers. Marx poked fun at the "abstinence" of the capitalist-employers and said that, if they found it too burdensome to save a part of what they were stealing from the workers, they should be kept from stealing in the first place. As he said:

The simple dictates of humanity therefore plainly enjoin the release of the capitalist from this martyrdom and temptation, in the same way that the Georgian slave-owner was lately delivered, by the abolition of slavery, from the painful dilemma, whether to squander the surplus product lashed out of his niggers, entirely in champagne, or whether to reconvert a part of it, into more niggers and more land<sup>20</sup>

A brief consideration reveals that, in this material, Marx has changed the subject and has given up for the moment his chosen task of describing the capitalistic system as it is. He is arguing now about the ethics of interest-receiving and is concluding that interest should not be paid for capital funds. Now the ethical arguments concerning the payment and receipt of interest are interesting and possibly important, but they are quite beside the point with which Marx is supposed to be dealing. If interest actually is paid for capital funds in a capitalistic system and has to be paid in that system, then any purported description of a capitalistic system which says that interest is not a cost of production is inaccurate and invalid, whether or not it is true, on ethical grounds, that interest should not be paid.

**Labor Which Produces No Value** While Marx insisted through thick and thin that the expenditure of labor-time was the sole cause of the natural values of commodities, he also held, interestingly enough, that some people expend a large amount of socially necessary labor-time without succeeding in creating either products or values. Such people are employers and workers in the field of exchange and merchandising. Said Marx:

The merchant performs a necessary function, because the process of reproduction itself includes an unproductive function. He works as well as any other man, but intrinsically his labor creates neither products nor values.<sup>21</sup>

Merchant's capital is simply capital performing its functions in the sphere of circulation. But no value is produced in the process of circulation and, therefore, no surplus value.<sup>22</sup>

The conversion of commodities (products) into money, and of money into commodities (means of production) is a necessary function of industrial capital, and therefore, a necessary operation for the capitalist. But these functions do not create any value, nor do they produce any surplus value.<sup>23</sup>

<sup>20</sup> *Ibid.*, p. 655

<sup>22</sup> Karl Marx, *Capital*, Volume III, p. 329

<sup>21</sup> Karl Marx, *Capital*, Volume II, p. 119

<sup>23</sup> *Ibid.*, p. 311

The same thing is true of workers employed by capitalists in this field. They perform socially necessary labor and receive wages, but create no products and no values. Apparently Marx followed the lead of the early classical economists on this point and considered labor productive only when it "created" some tangible physical product.

*What Kind of Value Was Marx Explaining?* Marx himself was conscious of some of the inadequacies of his theory of value as an analysis of what really goes on under capitalism. In fact, in the third volume of *Capital*, he finally admitted that commodities do not always sell for prices which correspond to the amount of labor-time embodied in them. This result he attributed to the different "organic composition of capitals" from one enterprise or industry to another. That is, all commodities would sell at values directly dependent upon the amount of labor-time embodied in them only under greatly simplified conditions of production in which there would be in all enterprises and industries an equal mingling of labor power, materials, and instruments of production.

However, the gaps and inconsistencies in Marx's basic theory of value are so great and obvious that many interpreters have felt the need to come to his assistance. In many cases, this assistance takes the form of contending that Marx was not trying to explain exchange-value in the ordinary sense at all. If Marx had been trying to explain ordinary exchange-value, he would have done a better job than he did. Thus, Cole says that when Marx seems to be talking about exchange-value he is really dealing with a kind of "objective use value." Objective use-value has nothing to do with use-value in the ordinary sense of utility. It is "what man adds by his efforts to what is conferred upon him by nature, so it is axiomatic that only human labor in some form can add value to the resources which are at man's disposal by sheer gift of nature"<sup>24</sup>. Many things other than labor can add to exchange-value or create it, but only labor, by definition, can create objective use-value.

This interpretation of Marx is not implausible, and, if it is valid, it obviously helps to clear up some of the inconsistencies in the Marxian theory of value. If value is what labor adds by its efforts to various natural objects, there is no question that labor is the only source of value. Land and other natural objects, before they

<sup>24</sup> G. D. H. Cole, *What Marx Really Meant*, p. 211. Reprinted by permission of Alfred A. Knopf, Inc., New York.

have been worked upon by labor, cannot possibly have any of this objective use-value, and can at any time have only the objective use-value conferred upon them by labor. Rare books, paintings, coins, stamps, and wines may have great exchange-value but their objective use-value can never exceed that conferred upon them originally by human labor. Interest may affect the money cost and exchange-value of commodities, but it can never affect their objective use-value since that is conferred by human labor alone, and so on.

However, while this interpretation helps out in some respects, it weakens or injures Marx's position in other respects. If Marx was dealing with this queer kind of value known as objective use-value in his theory of value, then it cannot be claimed that he succeeded in his attempt to describe and explain economic life under capitalism. Surely no description and analysis of economic affairs in a capitalistic system can be considered complete or accurate unless it comes to grips with exchange-values and their determination. Again, the interpretation of Marx's value as objective use-value weakens his famous exploitation thesis. The surplus value which the employers extort from their workers means, if it means anything at all, the difference between the income from the prices or values which the employers receive for their workers' products and the amount of income which the employers find it necessary to pay out in wages. And the prices which the employers receive from the sale of their workers' products are exchange-values not objective use-values. Surplus value, as a difference between the workers' actual wages and the mythical objective use-value of the workers' products, would be a rather meaningless concept. Thus, this interpretation of value proposed by Cole neatly transfers Marx from the frying pan to the fire.

### *Exposition of the Marxian Theory of Distribution*

**Distributive Shares** Ideally, the distribution of income should be very simple according to Marx. If labor actually creates all exchange value (as it does in the usual interpretation of Marx's theory of value), then all the income derived from the sale of the workers' products should revert to the workers. In actual practice, the workers receive only a part of the income derived from the sale of their products and the remainder goes to the capitalist-employers.

as surplus value After the surplus value is received, the capitalist-employers have great fun, according to Marx, in labeling various segments of it as rent, interest, and profits, but fundamentally these types of income are all surplus value Since surplus value is merely that share of the total income from the sale of goods which is not paid out in wages, the only task of the theory of income distribution is to explain the determination of wages All the rest is surplus value

*Labor and Labor-Power* In explaining wage determination, Marx found himself immediately in a dilemma Marx criticized other writers for "that nice and faulty circle, which makes the value of commodities arise out of the sum of the values of wages, profit, rent and the value of wages, profit, and rent, in their turn, is to be determined by the value of commodities, etc" <sup>25</sup> In the light of this attitude, he could hardly say that wages were paid for labor and depended on the value of the workers' products, since he had already said that the value of the workers' products depended upon labor, or the amount of labor-time embodied in them Marx avoided any difficulty of this kind by contending that labor, while it is the cause of the value of commodities, is not itself a commodity and has no value Wages are not paid for labor but for the use of the workers' labor-power

As Marx put it

Human labour-power in motion, or human labour, creates value, but is not itself value It becomes value only in its congealed state, when embodied in the form of some object <sup>26</sup>

And further

What the working man sells is not directly his labor, but his laboring power, the temporary disposal of which he makes over to the capitalist <sup>27</sup>

And still further

That which comes directly face to face with the possessor of money on the market, is in fact not labour, but the labourer What the latter sells is his labour power As soon as his labour actually begins, it has already ceased to belong to him, it can therefore no longer be sold by him Labor is the substance, and the immanent measure of value, but has itself no value In the expression, "value of labour," the idea of value is not only completely obliterated, but actually reversed It is an expres-

<sup>25</sup> Karl Marx, *Capital*, Volume III, p 985

<sup>26</sup> Karl Marx, *Capital*, Volume I, p 59

<sup>27</sup> Karl Marx, *Value, Price and Profit*, p 72

sion as imaginary as the value of the earth. What economists therefore call value of labour, is in fact the value of labour power, as it exists in the personality of the labourer, which is as different from its function, labour, as a machine is from the work it performs. The value of labour is only an irrational expression for the value of labour power.<sup>28</sup>

**Wage Determination** The nature of labor-power is relatively simple. As Marx said

By labour-power or capacity for labour is to be understood the aggregate of those mental and physical capabilities existing in a human being which he exercises whenever he produces a use-value of any description.<sup>29</sup>

Labor-power is bought and sold as a commodity and the problem is merely to determine its value or wage. Like other commodities, labor-power has a market value, determined by demand and supply, which fluctuates around its natural or real value. Marx, as usual, is interested primarily in natural or real value. He is also concerned only with the value of labor-power under modern conditions of production in which the worker is sole owner of his labor-power and is entirely free to sell it to the capitalist-employer, and in which the worker, being unable to produce and sell for himself commodities in which his labor-power is embodied, can exist only by offering his labor-power for sale as a commodity.

Under these conditions, the theory of wages or of the value of labor-power is merely an extension or corollary of the theory of value itself. Since labor-power is a commodity, its value or wage is determined, like that of any other commodity, by the quantity of labor-time required to produce it. The value of labor-power depends not on what labor-power produces but on what produces it. The wage is not a function of the labor-time which the worker spends in production but of the labor-time which is necessary to make the workers' labor-power available in production. And how much labor-time is required to produce the worker's labor-power? Well, the worker's labor-power will not be "produced" (that is, available for use in production) unless the worker is able to obtain at least minimum amounts of food, clothing, shelter, and other primary necessities of life. Moreover, from the long-term point of view, labor-power will not be available for the employer unless the workers are able to support families of necessary size for the maintenance of the labor supply from generation to generation.

<sup>28</sup> Karl Marx, *Capital*, Volume I, pp. 588-590.

<sup>29</sup> *Ibid.*, p. 186.

In the end, then, the amount of labor-time necessary to produce labor-power is the amount of labor-time required to produce the commodities and services necessary to the subsistence of the workers and their families, and natural wages, since they depend on the labor-time necessary to produce the labor-power, are subsistence wages. It is a popular short-cut to say that, in the Marxian analysis, wages are determined by subsistence, but this is not strictly accurate. Wages are determined by the amount of labor-time required to produce the worker's labor-power, and only work out incidentally to subsistence. If more than subsistence were required to make the worker's labor-power available in production, wages would amount to more than subsistence.

Thus, according to Marx, wages were determined entirely in the long run by the cost of production of labor-power in terms of labor-time. The strength of the demand for labor made no difference to wages. Whether the workers themselves produced much or little, whether their products had great or small exchange value, wages were unaffected so long as the amount of labor-time necessary to produce the labor-power did not change. Thus, said Marx:

The value of labour power is determined, as in the case of every other commodity, by the labour time necessary for the production, and consequently also the reproduction of this special article. In other words, the value of labour power is the value of the means of subsistence necessary for the maintenance of the labourer.<sup>20</sup>

And again

As with all other commodities, so with labor its *market price* will, in the long run, adapt itself to its value, that, therefore, despite all the ups and downs, and do what he may, the workingman will, on the average, only receive the value of his labor, which resolves into the value of his laboring power, which is determined by the value of the necessaries required for its maintenance and reproduction, which value of necessities finally is regulated by the quantum of labor wanted to produce them.<sup>21</sup>

In these and many other passages, Marx traces wages to the amount of labor-time required to produce labor-power and thence to the labor-time necessary to produce the subsistence of the workers.

*Differences in Wages Among Grades of Workers.* Since workers of all sorts would presumably need about the same quantities of

<sup>20</sup> *Ibid.*, pp. 189, 190.

<sup>21</sup> Karl Marx, *Value Price, and Profit*, pp. 115, 116.

commodities and services in order to subsist and reproduce their kind, and since, therefore, the amount of labor-time required to produce labor-power would be about the same for all workers, it would seem that the Marxian theory would provide a sort of dead level of wages for all workers. However, it is obvious that differences in wages abound in the actual capitalistic system and that these differences in wages are often particularly sharp as between different grades or groups of labor. Marx was able to explain these differences in wages to his own satisfaction and in a manner consistent with his other theories. Since there is only one source of value, it follows that, if some types of labor-power are worth more than others, it must be because more labor-time is expended in producing these types of labor-power. Only the amount of labor-time required to produce ordinary subsistence is necessary to make unskilled labor-power available for the market. Skilled labor-power, on the other hand, requires the expenditure of labor-time on ordinary subsistence and the expenditure of additional labor-time on the training of the labor-power. Hence, the wages of skilled workers are higher than those of unskilled workers only by an amount which represents the extra labor-time required to train the skilled workers. Since various types of skilled workers require different amounts of training, Marx could account for large numbers of differences in wages in this way.

Thus, Marx said

'All labour of a higher or more complicated character than average labour is expenditure of labour power of a more costly kind, labour-power whose production has cost more time and labour, and which therefore has a higher value, than unskilled or simple labour-power.'<sup>82</sup>

This explanation of differences in wages clearly makes no allowance for any differences in wages based on differences in the natural abilities or talents of the various workers. It implies that basically all labor is really of a single grade, and that workers differ from each other in the end only because some workers receive training and others do not. It implies also that we can readily make labor of any required degree of skill out of common or unskilled labor simply by providing extensive training. If we have an unskilled worker and need a doctor or scientist, all we need to do is give our raw material enough training. All this is consistent, of course, with

<sup>82</sup>- Karl Marx, *Capital*, Volume I, p. 220.

Marx's general theory of value Marx had held that land and other objects in a purely natural state could have no value, since labor-time (the source of all value) had not been expended on them If this is true, then the talents and abilities of people, in so far as they too are purely natural in character can have no value (and can command no wage differentials) so long as labor-time has not been expended on them Moreover, just as land and other natural objects, once labor-time had been expended in developing them, could have value only in proportion to the amount of labor-time embodied in them, so too the natural talents and abilities of people, having been developed by the expenditure of labor-time in their training, could obtain extra wages only in proportion to the labor-time devoted to their training It would have been hopelessly inconsistent for Marx to have attributed differences in wages to the fact that some workers had natural talents and abilities which other workers lacked, after having denied value to land and other purely natural objects

### *Criticism of the Marxian Theory of Distribution*

*The Distributive Shares* The Marxian theory of distribution, on the whole, is most unsatisfactory The division of total income into only two shares, the one (wages) functional as a payment for the labor-power of workers and the other (surplus value) nonfunctional and resulting from the exploitation of the workers, is useful for Marx's revolutionary purposes, but nothing more can be said in favor of it The lumping together of three types of income (rent, interest, and profit) into surplus value, while ridiculing the thought that any genuine differences can exist between them, is consistent with the rest of the Marxian theoretical analysis, but from the point of view of modern economic theory it is one degree more confused than the classical economists' practice of combining interest and profits into a catch all type of income which included all income which was not wages and rent The notion that rent, interest, and profits are all derived from the exploitation of the workers may be desirable for the purpose of rabble-rousing, but it shows very little understanding of the functioning of the productive agents

*The Neglect of Demand* In general, the Marxian theory of wages is open to some of the same objections which were noted in connection with the theory of value The theory that the wages paid for labor-power are determined solely by the amount of labor-time

necessary to produce, maintain, and train the labor-power shows the usual rather complete Marxian neglect of the demand factor. It hardly seems possible that anyone could have undertaken to explain wages without paying any attention to the demand for labor of various kinds, the quantities of products which the workers can turn out, and the exchange-values which these products have on the market. According to the Marxian theory, two workers who required the same quantities and kind of commodities and services to maintain themselves and their families would apparently receive the same wages, even if one worker could turn out twice as much product per day or per week as the other worker. Again, two workers who had the same subsistence needs for themselves and their families would presumably receive the same wages even though the product of the one worker was actively demanded on the market and had great exchange-value while the product of the other worker was not much in demand and had little exchange-value.

Of course, Marx could argue that the latter situation would take care of itself in the long run. That is, capitalists hire workers not merely to create some exchange-value but to create as much exchange-value as possible. If, therefore, workers of the same grade and receiving the same wages create products of much greater exchange-value in one industry than in another, employers will presumably shift from the latter industry to the former in the long run, and this transfer would continue until the workers in both industries were creating equivalent amounts of exchange-value. This, however, would not solve the problem of the wages of workers of the same grade in the same industry who, because of differences in personal industriousness or other qualities, turned out widely varying quantities of product. Such workers, on the basis of a simple supply theory of wages, would apparently get the same wages based upon the amount of labor-time necessary to create the labor-power, unless they had varying needs for subsistence.

Again, Marx had said in connection with the theory of value that, if an article produced by labor is useless, so is the labor which produced it. Such labor does not count as labor and therefore creates no value. However, according to the theory of wages, if anyone is foolish enough to employ labor which creates commodities that are not in demand and have no exchange-value, the labor-power of these workers can apparently command wages as great as those received by other workers with the same subsistence needs.

since wages are not related to the value of the workers' products. All these things indicate that it is just as difficult to account for wages solely in terms of the labor-time spent in producing the labor-power as it is to account for the value of commodities solely in terms of the labor-time spent in producing them. Adequate explanations in both cases require an emphasis on demand as well as on supply. However, in the case of wage theory as in the case of value theory, Marx undoubtedly depended to a considerable extent on the writings of the earlier classical economists, and these economists had also shown quite a strong bias toward a subsistence theory of wages.

*The Neglect of Scarcity.* Again, we must object to the Marxian notion that differences in wages between skilled and unskilled workers can be accounted for in terms of the greater labor-cost of producing the labor-power of the skilled workers, since these workers require both subsistence and training while the unskilled workers require only subsistence. We do not deny that varying costs of training affect money wages. In fact, differences in the cost of training are commonly advanced today as one explanation of the differences in wages which exist between occupations which are open to workers of a given grade or group. But differences in the cost of training, or the fact that training is needed in one case and not in the other, cannot be used as the sole explanation of differences in wages between the various grades or groups of labor. The modern explanation is, of course, that skilled workers and professional workers receive higher wages than unskilled workers because of their greater marginal productivity. This varying productivity (a demand factor) is in turn dependent upon differences in the numbers of workers available for these different types of work. Many workers are available for unskilled tasks while relatively few workers are available for skilled and professional work. Finally, these differences in numbers are attributable to the fact that a variety of hereditary factors and environmental factors (including cost of training) prevent the movement of workers from the unskilled group to the skilled and professional groups. This explanation clearly indicates how greatly Marx overemphasized the factor of cost of training. Wage data also indicate the absurdity of the Marxian position. It is obviously impossible to account for the great gulf which exists between the wage of the worker in a routine machine-tending job and the wage of a hired manager of the plant solely in terms of the greater cost of the

training received by the manager or the labor-time devoted to such training.

The Marxian explanation implies also that he was a thorough-going believer in the effects produced by environment. That is, his explanation implies that labor is basically all of one grade except for differences in training, and that labor of any degree of skill can be produced from common labor simply by the application of adequate training. Even today, there are some people who would agree with Marx on this point. They contend that any person who is not actually deficient in intelligence can be made into a doctor, a lawyer, a virtuoso of the piano or violin, a business enterprise, an industrial manager, or anything else, if he can be taken over at a very early age and given an appropriate environment and training. On the other hand, there are many supporters of Marx who find his theory on this point somewhat objectionable. Cole, for example, says that the notion that the respective values of different kinds of labor coincide with the values which must be used in order to produce an adequate supply of each kind would be completely true only if all kinds of human skill and productivity were producible at will like commodities.<sup>33</sup>

There is, of course, some element of truth in the Marxian position. Training, whether conceived of in terms of labor-time devoted to it or otherwise, may be considered perhaps the chief factor involved in converting unskilled workers into semi-skilled workers, or either of these types of workers into skilled workers, and natural differences between workers in these groups may be relatively slight. On the other hand, professional, managerial, and entrepreneurial workers do not seem to us to be just ordinary workers who have received large amounts of training. The high wages which these types of workers receive in comparison with those received by workers in the lower groups can perhaps be attributed in part to superior training and other environmental factors, but they must also be attributed in part to natural talents and abilities which training alone can neither produce nor replace. Natural talents and abilities, like other scarce, useful, natural things, seem to command a price and have a value in any actually operating capitalistic system. We may concede, however, that Marx could not take this position of ours with respect to differences in wages without abandoning to that extent his general dictum to the effect that the expenditure of

<sup>33</sup> G D H Cole, *What Marx Really Meant*, pp. 222-223.

labor-time is the cause of all value, whether of commodities or of labor-power.

*The Varying Meaning of Subsistence.* A final objection to the Marxian theory of wages points out that Marx could never completely make up his mind as to the meaning of subsistence. In many passages, Marx states very definitely that the wages of ordinary workers depend upon the amount of labor-time required to produce the workers' labor-power, that this amount of labor-time is the same as that necessary to produce the commodities and services which are required for the maintenance of the workers and their families, and that maintenance is to be interpreted as bare physical subsistence. In many other passages, however, subsistence is interpreted to mean something closely akin to the modern concept of standard of living, or that customary quantum of commodities and services without which, whether or not they are necessary to physical existence, the individual thinks he cannot get along. For example, Marx states

'The value of labour power is determined by the value of the necessities of life habitually required by the average labourer.<sup>34</sup>

His means of subsistence must therefore be sufficient to maintain him in his normal state as a labouring individual.<sup>35</sup>

In contradistinction therefore to the case of other commodities, there enters into the determination of the value of labour-power a historical and moral element.<sup>36</sup>

Besides this mere physical element, the value of labor is in every country determined by a traditional standard of life. It is not mere physical life, but it is the satisfaction of certain wants springing from the social conditions in which people are placed and reared up. This historical or social element, entering into the value of labor, may be expanded, or contracted, or altogether extinguished so that nothing remains but the physical limit. By comparing the standard wages or values of labor in different countries and by comparing them in different historical epochs of the same country, you will find that the value of labor itself is not a fixed but a variable magnitude.<sup>37</sup>

How can we explain Marx's wavering back and forth between the "physical subsistence" and "standard of living" interpretations of wages and subsistence? The answer seems to be that either inter-

<sup>34</sup> Karl Marx, *Capital*, Volume I, p. 568.

<sup>35</sup> *Ibid.*, p. 190.

<sup>36</sup> *Ibid.*, p. 190.

<sup>37</sup> Karl Marx, *Value, Price, and Profit*, pp. 117-119.

pretation left something to be desired from Marx's point of view. The interpretation of wages in terms of strict physical subsistence was excellent for the purpose of Marx's exploitation thesis. If the wages of ordinary labor are held at the level of strict physical subsistence by something akin to a natural law, the position of the workers under capitalism seems hopeless. That is, wages cannot be bid up by either workers or employers any more than fishermen or their customers can bid up the tides. Moreover, exploitation of the workers is inevitable. The workers can produce an amount of value equal to their wages or subsistence with just a few hours of work, but the capitalist-employers, since by paying wages they acquire the right to use the workers' labor-power at their discretion, can keep the workers busily at work for many hours each day after they have earned their daily subsistence wages. All the exchange-value of commodities which the workers produce in excess of the exchange-value of the commodities and services which make up their subsistence is surplus value and goes to swell the ill-won gains of the capitalist-employers.

While the interpretation of wages in terms of bare physical subsistence was ideal from this point of view, it was unsatisfactory in other respects. For one thing, it did not square with the facts. Even in the capitalistic system of Marx's day, it was obvious that there were large numbers of workers whose wages could not be accounted for in terms of bare physical subsistence or even in terms of physical subsistence plus the cost of training. Again, if there is some natural law which sets the wages of ordinary labor at the level of physical subsistence, what grounds do we have for expecting that wages will be higher in some other noncapitalistic system? Perhaps this is a peculiar kind of natural law which operates only in a capitalistic economic system, and workers will be able to obtain more than the real or natural value of their labor-power in some other system.

The interpretation of the wages of ordinary workers in terms of standard of living seems to fit the facts of wage payment in a capitalistic system better than the interpretation in terms of physical subsistence, and it offers some hope of ameliorating the workers' position. The drawback of this interpretation is that it greatly weakens Marx's exploitation thesis. If wages are not determined by natural law and if workers can induce an increase in their wages by coming to regard certain commodities and services as indispensable

to their continued functioning, even though these same economic goods are not necessary to their physical subsistence, then wages are flexible and can be bid up even in a capitalistic system. And if wages can be bid up to some extent, there seems to be no logical reason why they cannot be bid up to the point at which the workers receive the entire value of their contribution to production and there is no surplus value for the employer or exploitation of the workers. The nature of Marx's dilemma in interpreting wages and subsistence is apparent.

Some interpreters of Marx reach the conclusion that Marx decided on the standard of living as the true interpretation of the wages or subsistence of ordinary workers, and these people argue that this interpretation not only is in accord with the facts of economic life but does not really weaken Marx's exploitation thesis. According to this view, workers could not bid up their wages and exhaust the surplus value received by the capitalist employers. In the first place, the bargaining power of the workers is too weak in relation to that of the employers. Again, a rising price for labor-power would limit its use, bring about unemployment, lower the workers' bargaining power, and cause a revaluation of the products of the workers. These arguments seem rather objectionable to us. If the workers were already receiving their full marginal productivity, an attempt to get a still higher wage might limit the use of labor and affect employment adversely. But why should a rising wage produce unemployment if in the original situation the employers were not giving the workers their full marginal productivity but were making enormous profits or surplus value from the employment of each worker? Why should rising wages cause any revaluation of the workers' products if the exchange-value of these products depends solely upon the amount of labor-time embodied in them and not at all upon the size of the wages paid to the workers?

In any case, we do not have to rely on the workers to bid up wages under capitalism, for, under the competitive conditions which Marx assumes, the employers should take the matter into their own hands if wages are flexible. Suppose, for example, we take an employer who is using 100 workers and is making tremendous profits or surplus value from their use. He works them 12 hours per day but pays them only for 6 hours, since 6 hours of labor-time are enough to produce their subsistence. With a margin of 100 per cent

of surplus value being made on each worker, would this employer not like to hire additional workers and make an even greater total of surplus value? Would he not attempt to get additional workers even if he had to bid them away from other employers by offering higher wages? He could offer wages equal to the value of 7 or 8 hours of work and still retain a good margin of profit on each worker. Four or five hours' worth of surplus value from each of 200 workers would be better than 6 hours' worth of surplus value from each of only 100 workers. The employer would not have to be concerned about lowering the value of his finished product, since, as one enterpriser in a competitive industry, he could increase or decrease his output without affecting the general value of the product on the market. With each employer in the same situation and figuring in the same way, with each employer trying to get additional workers to increase his total surplus value and trying to retain the workers already in his employ, it would seem that wages would be bid up until no employer had any incentive to attract additional workers away from other employers. This point would be reached when the workers were receiving wages which equalled the value of their contribution to production and there was no surplus value to be made by the employers. We are inclined to think, therefore, that the interpretation of wages as flexible, in combination with competitive conditions in industry, would have to be regarded as fatal to Marx's exploitation thesis.

The generally accepted opinion is that Marx, whenever pressed to the wall, fell back on his interpretation of wages in terms of bare physical subsistence and held that any forces which tend to remove wages from the level of physical subsistence operate either temporarily or so slowly that their influence may be neglected for all practical purposes. Marx's inclination in this matter was natural, and most other people in his position would have acted in the same way. If one is faced with a choice of two interpretations, one of which is more consistent with the facts of economic life but is decidedly in conflict with one's pet theories and the other of which is somewhat deficient in realism but is most useful in connection with one's purpose in attempting an analysis of economic affairs, the latter interpretation is likely to be selected. But Marx did make occasional bows in the direction of the standard of living interpretation.

## QUESTIONS

- 1 'Marx held that the natural values of commodities could not be determined by demand and supply conditions' Explain
- 2 'In explaining the natural values of commodities, Marx rejected use value or utility as a subjective and relative concept' Explain
- 3 How did Marx use the concepts of "socially necessary labor" and "standard time units of unskilled labor" in his value theory?
- 4 Explain how Marx, in developing his theory of value, handled the problems implicit in (a) differences in labor time from one producer to another under a given state of the arts of production, (b) differences between original and reproduction cost in terms of labor time, and (c) differences in the grades of labor required to produce a good
- 5 How did Marx dispose of land and capital in reaching his conclusion that the natural values of commodities are determined by their content of socially necessary labor time?
- 6 "One of the most serious criticisms of the Marxian theory of value is found in the fact that Marx greatly minimized, if he did not actually overlook, the part played by demand in determining the exchange values of commodities" Explain
- 7 "In developing his theory of value, Marx missed an excellent opportunity to employ his basic philosophy involving thesis, antithesis, and synthesis" Explain
- 8 "The Marxian theory of value is open to criticism because of the treatment which Marx accorded to the factor of scarcity" Show whether you agree
- 9 "The Marxian theory of value based on labor time, though severely criticized by economists, does not differ significantly from the modern theory of value with its emphasis on cost of production" Do you agree? Explain
- 10 "In his treatment of capital as a factor in relation to the values of commodities, Marx temporarily gave up his chosen task of describing the capitalistic system as it is" Explain
- 11 "In suggesting that Marx was not really trying to explain exchange values in the ordinary sense, the supporters of Marx merely leap from the frying pan into the fire" Show whether you agree
- 12 You are asked by the local Kiwanis Club to make a speech before its members showing what is wrong with the Marxian theory of value from the point of view of modern economics Indicate what you would say on this subject
- 13 "The Marxian theory of value was defective in that it omitted (a) the part played by demand in determining value, (b) the significance of capital goods in connection with production and costs, (c) the influence of natural scarcity on value, and (d) the fact that saving

and waiting are necessary in order that capital goods may be created" Discuss the validity of these criticisms of the Marxian theory of value

- 14 "The Marxian theory of the distribution of income was greatly oversimplified" Show whether you agree
- 15 Distinguish between labor and labor-power as these terms were used in the Marxian analysis
- 16 "Marx's theory of wages was merely a logical extension of his general theory of value" Show whether you agree
- 17 "While the Marxian theories of value and wages are usually stated separately, they are really only a single theory" Explain
- 18 How did Marx account for differences in wages between different grades of labor? Explain
- 19 How would you criticize the Marxian theory of wages in the light of modern economics?
- 20 "The Marxian theories of value and wages are subject to the same general criticisms" Show whether you agree
- 21 "Marx apparently had a difficult time in making up his mind as to the exact meaning which should be attached to the term 'subsistence' in his wage theory" In interpreting this statement, explain (a) the two ways in which Marx sometimes defined the term "subsistence," (b) the difficulties which he encountered with each of these definitions, and (c) the final choice which he made between the two meanings and why he made this selection

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CHAPTER 28

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**THE MARXIAN THEORY OF  
SURPLUS VALUE**

The theory of surplus value is the climax toward which the theories of value and wages have been building. While the theory of surplus value, as explained in detailed fashion by Marx, is troubled by its own errors and inconsistencies, it is nevertheless possible to say that this theory in general follows logically and inevitably from the theories of value and wages. If these theories are true, the workers are exploited and the employers receive surplus value. It has been impossible to present the Marxian theories of value and wages without suggesting the general nature of the theory of surplus value, but we need now to investigate and analyze this latter theory in some detail.

*Exposition of the Theory of Surplus Value*

*Assumptions of the Theory* The theory of surplus value, in the first place, rests on a number of assumptions. The workers are assumed to be free men and not slaves. They are the sole owners of their labor-power and are completely qualified to sell it as a commodity on the market. The workers, since they lack the necessary land and capital, are unable to use their labor-power directly to make commodities which they can sell, and hence must dispose of their labor-power as a commodity to the capitalist employers who own or control the necessary non-human factors of production.

In order to become a commodity, a use value must be a non-use value for its owner. Labor power must also be a non-use value for the worker, if it is to appear in the market as a commodity. If the worker has access to the means of production, he does not sell his labor power, but employs it himself, and sells his products.<sup>1</sup>

<sup>1</sup> Karl Kautsky, *The Economic Doctrines of Karl Marx*. London: A & C Black Ltd., 1925, p. 60.

When the worker sells his labor-power to the employer, he gives up all title and claim to the products of his labor. When the worker produces a product, it belongs entirely to the employer who will dispose of it on the market as best he can. Finally, it is assumed that the worker, in selling his labor-power to the employer, confers on the employer the right to use this labor-power to best advantage. This means, in effect, that the length of the working day is set by the employer, and not by the worker or by agreement between employer and worker. When there are no legal limitations on the length of the working day, the employer's decision in this matter is limited only by self-interest and custom. The employer knows that, if he attempts to use the worker's labor-power for twenty-four hours today, he may not get another chance to use this worker's labor-power for three or four days thereafter. However, the worker may be able to manage sixteen hours day after day over a long period. In this fashion, the length of the working day is regulated to some extent by the employer's self-interest. It is also regulated by custom and tradition. As Marx says

By selling his laboring power, and he must do so under the present system, the workingman makes over to the capitalist the consumption of that power, but within certain rational limits. He sells his laboring power in order to maintain it, apart from its natural wear and tear, but not to destroy it. In selling his laboring power at its daily or weekly value, it is understood that in one day or one week, that labouring power shall not be submitted to two days' or two weeks' waste or wear and tear. Machinery does not wear out exactly in the same ratio in which it is used. Man, on the contrary, decays in a greater ratio than would be visible from the mere numerical addition of work.<sup>2</sup>

**The Theory Stated** Under these conditions, the worker sells his labor-power as a commodity to a capitalist-employer and, in the average case, receives a price or wage for it which is based on the amount of labor-time required to produce the labor-power, or the amount of labor-time socially necessary to produce subsistence or maintenance (including training) for the worker and his family. Let us suppose that this subsistence requires five hours of socially necessary labor-time daily for its production. Then, if the worker labored only five hours daily for his employer, he would be fully paid and there would be no surplus value. However, it is the employer's right to set the length of the working day, and he will normally set it at a number of hours greater than that required to produce the

<sup>2</sup> Karl Marx, *Value, Price, and Profit*, pp. 107-108.

worker's subsistence Let us assume, for example, that the worker puts in ten hours daily at his task The worker's product belongs to the employer, and he will sell it on the market for its full value If the worker is of average efficiency, his daily product will sell for a price based on the ten hours of labor-time which the worker puts in The difference between the value of the product created daily by the worker (based on ten hours of labor-time) and the value returned to him daily in wages (based on five hours of labor-time) is value produced by the worker but received and retained by the employer In other words, it is surplus value

Obviously, there are several ways in which the surplus-value relationship may be expressed The difference between the exchange-value created by a worker in a day and the exchange-value of the commodities and services necessary to the subsistence of the worker and his family for a day is the exchange-value which is surplus value The difference between the number of hours of work put in by a worker in a day and the number of hours of work necessary to produce subsistence for the worker and his family is the number of hours for which the worker is uncompensated and during which the worker is producing surplus value for the employer The difference between the quantity of commodities produced by the worker in a day and the quantity of commodities necessary to the subsistence of the worker and his family is the quantity of commodities whose value is surplus value And so on However the relationship is expressed, the worker produces more value than he receives, and he is exploited by the employer The income of the employer is derived from the uncompensated labor of the worker

Of course, the whole surplus value is not always kept indefinitely by the enterpriser, or employer of labor As Marx says

The monopoly of land enables the landlord to take one part of that surplus value under the name of rent, whether the land is used for agriculture buildings or railways, or for any other productive purpose On the other hand, the very fact that the possession of the instruments of labor enables the employing capitalist to produce a surplus value, or, what comes to the same, to appropriate to himself a certain amount of unpaid labor, enables the owner of the means of labor, which he lends wholly or partly to the employing capitalist—enables, in one word, the money lending capitalist to claim for himself under the name of interest another part of that surplus value, so that there remains to the employing capitalist as such only what is called industrial or commercial profit By what laws thus division of the total amount of surplus value amongst

the three categories of people is regulated is a question quite foreign to our subject This much, however, results from what has been stated

*Rent, Interest, and Industrial Profit* are only different names for different parts of the surplus value of the commodity, or the unpaid labor enclosed in it, and they are equally derived from this source, and from this source alone They are not derived from land as such or from capital as such, but land and capital enable their owners to get their respective shares out of the surplus value extracted by the employing capitalist from the laborer For the laborer himself it is a matter of subordinate importance whether that surplus value, the result of his surplus labor, or unpaid labor, is altogether pocketed by the employing capitalist, or whether the latter is obliged to pay part of it, under the name of rent and interest, away to third parties Suppose the employing capitalist to use only his own capital and to be his own landlord, then the whole surplus value would go into his pocket<sup>3</sup>

*A Marxian Illustration of Surplus Value* In order to guard against any possible danger of misstatement, we present the following illustration of the creation of surplus value from Marx's Value, Price, and Profit.

Now suppose that the average amount of the daily necessities of a laboring man require six hours of average labor for their production Suppose, moreover, six hours of average labor to be also realized in a quantity of gold equal to 3 s Then 3 s would be the Price, or the monetary expression of the Daily Value of that man's Laboring Power If he worked daily six hours he would daily produce a value sufficient to buy the average amount of his daily necessities, or to maintain himself as a laboring man

But our man is a wages laborer He must, therefore, sell his laboring power to a capitalist If he sell it at 3 s daily or 18 s weekly, he sells it at its value Suppose him to be a spinner If he works six hours daily he will add to the cotton a value of 3 s daily This value, daily added by him, would be an exact equivalent for the wages, or the price of his laboring power, received daily But in that case no surplus value or surplus produce whatever would go to the capitalist Here, then, we come to the rub

In buying the laboring power of the workman, and paying its value, the capitalist, like every other purchaser, has acquired the right to consume or use the commodity bought You consume or use the laboring power of a man by making him work, as you consume or use a machine by making it run By buying the daily or weekly value of the laboring power of the workman, the capitalist has, therefore, acquired the right to use or make that laboring power work during the whole day or week The working day or the working week has, of course, certain limits, but those we shall afterwards look more closely at

For the present I want to turn your attention to one decisive point

<sup>3</sup> *Ibid.*, pp. 89-91

The value of the laboring power is determined by the quantity of labor necessary to maintain or reproduce it, but the use of that laboring power is only limited by the active energies and physical strength of the laborer. The daily or weekly value of the laboring power is quite distinct from the daily or weekly exercise of that power the same as the food I have in my possession and the time it can carry the horseman are quite distinct. The quantity of labor by which the value of the working man's laboring power is limited forms by no means a limit to the quantity of labor which his laboring power is apt to perform. Take the example of our spinner. We have seen that, to daily reproduce his laboring power, he must daily reproduce a sum of three shillings, which he will do by working six hours daily. But this does not divide him from working ten or twelve or more hours a day. But by paying the daily or weekly value of the spinner's laboring power the capitalist has acquired the right of using that laboring power during the whole day at week. He will, therefore, make him work in, daily twelve hours. Over and above the six hours required to replace his wages or the value of his laboring power, he will, therefore, have to work in other hours which I shall call hours of surplus labor, which surplus labor will realize itself in a surplus value and a surplus produce. If our spinner, for example, by his daily labor of six hours adds three shillings' value to the cotton, a value forming in exact equivalent to his wages, he will, in twelve hours, add six shillings worth to the cotton, and produce a proportional surplus of yarn. As he has sold his laboring power to the capitalist, the whole value or produce created by him belongs to the capitalist the owner *pro tem* of his laboring power. By advancing three shillings the capitalist will, therefore, realize a value of six shillings, because advancing a value in which six hours of labor are crystallized he will receive in return a value in which twelve hours of labor are crystallized. By repeating this same process daily, the capitalist will daily advance three shillings and daily pocket six shillings one half of which will go to pay wages anew and the other half of which will form surplus value, for which the capitalist pays no equivalent. It is this sort of exchange between capital and labor upon which capitalistic production, or the wages system, is founded and which must constantly result in reproducing the working man as a working man and the capitalist as a capitalist.

*The rate of surplus value, all other circumstances remaining the same, will depend on the proportion between that part of the working day necessary to reproduce the value of the laboring power and the surplus time or surplus labor performed for the capitalist. It will therefore, depend on the ratio in which the working day is prolonged over and above that extent, by working which the working man would only reproduce the value of his laboring power, or replace his wages.*<sup>4</sup>

*Other Considerations* Marx clearly intimates that the creation of surplus value is an inevitable characteristic of a capitalistic eco-

<sup>4</sup> *Ibid.*, pp. 77-81.

nomic system Since the worker has no way of using his own labor-power to produce commodities, he must sell his labor-power to the capitalist-employer for a subsistence wage if he wishes to go on living, and the urge to live is strong in most people. There is no way in which the worker can avoid the bad bargain which he makes with the employer—a bargain which causes the worker to create much more value for the employer than he receives in wages. Of course, there is no law which says that the capitalist-employer must exploit his workers, and keep them busy more hours per day than would be necessary to replace their wages, unless it is the law of self-preservation. However, the employer would be foolish not to exploit his workers, for he would lack any visible means of support if he kept the workers busy only enough hours per day to replace their wages. As we have seen, Marx divided the total income of the capitalist-employer into only two parts, one necessary to give him back the wages which he has paid to the workers and the other consisting of surplus value. If he received no surplus value, he would apparently have no income for himself. If the capitalist-employer received no income for himself, it is difficult to see how he could survive, and he would certainly have no incentive to keep on operating his land and capital in production.

The capitalist-employer must not only operate his business so that he receives surplus value, but he must also exploit his workers as thoroughly as other capitalist-employers do. If he becomes soft-hearted, lets up on his workers, and secures less surplus value than his competitors, he weakens his own relative financial position. When a severe business depression comes along, he is then less likely to survive than his more rapacious competitors and is likely to be forced to the wall. Thus, the capitalist-employer who hesitates to exploit his workers to the full is likely to find himself a member of the exploited group, instead of being one of the exploiters, before many years have passed.

We should also note that surplus value does not result from selling the products of labor for more than they are worth or from paying the workers less than their labor-power is worth. Temporary fluctuations of wages and prices around their long-run norms may temporarily increase or decrease the amount of surplus value received by the employer, but in the long run the employer receives abundant surplus value even though he sells the products of labor at their real or natural value and buys labor-power at its real or

natural value, as these values are determined in a capitalistic system As Marx says

The value of a commodity is determined by the *total quantity of labor* contained in it But part of that quantity of labor is realized in a value, for which an equivalent has been paid in the form of wages, part of it is realized in a value for which no equivalent has been paid Part of the labor contained in the commodity is *paid labor*, part is *unpaid labor* By selling, therefore, the commodity *at its value*, that is, as the crystallization of the *total quantity of labor* bestowed upon it, the capitalist must necessarily sell it at a profit He sells not only what has cost him an equivalent, but he sells also what has cost him nothing, though it has cost his workmen labor The cost of the commodity to the capitalist and its real cost are different things I repeat, therefore, that normal and average profits are made by selling commodities not above, but at their real values<sup>5</sup>

One is almost moved to wonder how a capitalist-employer could ever fail and be forced to go out of business

We should avoid the notion, which some people have concerning surplus value, that it results from shady or dishonest dealing on the part of the employer or at the very least from his being greedy and grasping As a matter of fact, the employer is just as much a tool of the capitalistic system as is the exploited worker He does only what he must do in order to survive and play his part in the capitalistic system Moreover, if we selected a number of workers at random and put them in the places of the present capitalist-employers, they would behave exactly as the present incumbents do Surplus value results from the legitimate exercise of the rights which the capitalistic system grants to the capitalist-employer Thus Marx said

Suppose that a capitalist pays for a day's labour-power at its value, then the right to use that power for a day belongs to him, just as much as the right to use any other commodity, such as a horse that he has hired for the day To the purchaser of a commodity belongs its use, and the seller of labour-power, by giving his labour, does no more in reality, than part with the use value that he has sold By the purchase of labour-power, the capitalist incorporates labour, as a living ferment, with the lifeless constituents of the product The product of this process also belongs, therefore, to him, just as much as does the wine which is the product of a process of fermentation completed in his cellar<sup>6</sup>

Surplus value results from a bad economic system, and not from bad employers

<sup>5</sup> *Ibid.*, pp. 87-88

<sup>6</sup> Karl Marx, *Capital*, Volume I, p. 206

*Ancient and Modern Surplus Value* According to Marx, the toiling masses have always been exploited by some other class. However, in former times the exploitation was open and aboveboard, while now it is concealed by the wage system. When the serf in medieval times worked some days for himself on his own land and some days for his lord on the latter's land, he was exploited beyond any doubt, but anyone could then see that part of the serf's labor benefited himself while the remainder was for the benefit of the lord. There was no concealed exploitation. In similar fashion

In slave-labour, even that part of the working day in which the slave is only replacing the value of his own means of existence, in which, therefore, in fact, he works for himself alone, appears as labour for his master. All the slave's labour appears as unpaid labour. In wage-labour, on the contrary, even surplus labour, or unpaid labour, appears as paid. There the property-relation conceals the labour of the slave for himself, here the money-relation conceals the unrequited labour of the wage-labourer.<sup>7</sup>

*Constant and Variable Capital* The Marxian illustrations of surplus value suggests usually that the employer just about doubles his money when he hires labor-power at its natural value and sells the workers' products for their natural value. However, it should be noted that the money which is doubled is not the total capital of the capitalist-employer but merely that part of his capital which he uses for paying wages to his workers. Marx divides the capital of an enterprise into two parts called constant capital and variable capital. Constant capital includes factories, plants and other buildings, tools and machinery, raw materials and supplies, partly finished goods, and even finished products in the hands of the producers—in fact, all sorts of capital goods, but not land. Such things are called constant capital because their value as a whole remains constant throughout the process of production. Such capital produces no surplus value, for it is the product of past labor. When the capital was produced, the labor which produced it was exploited no end, but that labor has escaped by now and cannot be exploited further in the present.

The best that constant capital can do is to replace itself or reproduce its own value over its lifetime. In fact, Marx does not explain clearly how it can do that much, but contents himself with saying that constant capital is bought, and sold (through its final products), at its value. Thus, he says

<sup>7</sup> *Ibid.*, p. 591

The means of production never transfer more value to the product than they themselves lose during the labour-process by the destruction of their own use-value. However useful a given kind of raw material, or a machine, or other means of production may be, though it may cost £150, or, say, 500 days' labour, yet it cannot, under any circumstances, add to the value of the product more than £150.<sup>5</sup>

The capitalist-employer cannot possibly "exploit" his factories and his machines.

On the other hand, variable capital is that part of an enterprise's capital which finds investment in labor-power and is used to pay wages. In terms of physical goods, it takes the form of food, clothing, shelter, and other necessaries of subsistence which are consumed by the workers. Such capital is called variable because, by investing it in labor-power, the employer is able to recapture not only the amount paid out but an additional sum called surplus value. Marx concludes naturally that surplus value is derived entirely from variable capital. Since the expenditure of labor-time produces all value, and since the labor-power which expends the value creating labor-time is bought with variable capital, the expenditure of variable capital really "purchases" surplus value and the amount of surplus value must be proportional to the expenditure of variable capital.

*The Rates of Surplus Value and Profit* On the basis of these considerations, Marx also distinguishes between the rate of surplus value and the rate of profit which an enterprise achieves. The rate of surplus value is the amount of surplus value received by the capitalist-employer in a year (or other period of time) as a percentage of the variable capital expended in the same period. On the other hand, the rate of profit is the same quantity of surplus value expressed as a percentage of the total capital of the enterprise, including both variable and constant capital. Or, as Marx put it

The rate of surplus value measured by the variable capital is called rate of surplus value. The rate of surplus value measured by the total capital is called rate of profit.<sup>6</sup>

*The Declining Rate of Profit* The distinctions between constant and variable capital, and between rate of surplus value and rate of profit, led Marx to his famous conclusion that the rate of profit

<sup>5</sup> *Ibid.* pp. 227-229.

<sup>6</sup> Karl Marx, *Capital*, Volume III, p. 55.

received by a capitalist-employer tends to decline as his enterprise increases in size and has an increasing proportion of its total capital take the form of constant capital. This does not mean that the workers are exploited less than before or that the rate of surplus value is less than before. The rate of surplus value (surplus value divided by variable capital) may be constant, or even increasing if the employer finds it necessary to exploit his employees more than formerly, but the rate of profit (surplus value divided by total capital) tends to decline as the business increases in size and a greater and greater proportion of its total capital consists of that constant capital which produces no surplus value.

This notion of the declining rate of profit got Marx into serious difficulties. He had trouble in explaining why enterprisers seek to increase the size of their firms and why they invest heavily in machinery and increase the proportion of constant capital to variable capital. And he had even more trouble in explaining why the large-scale firms which had already been set up in his day apparently did very well for themselves in the matter of profits. Nevertheless, he made a desperate effort to stick to his guns. For example, he said

- ✓ If a capital, consisting of percentages of 90C [Constant] and 10V [Variable], produced as much surplus-value, or profit, with the same degree of exploitation, as a capital consisting of percentages of 10C and 90V, then it would be as plain as daylight that the surplus-value, and value in general, must have an entirely different source than labor, and that political economy would then be without a rational basis.<sup>10</sup>

*Ways of Increasing Surplus Value* Since each capitalist-employer, if he is to survive, must be sure to make as much surplus value as his competitors and would prefer to be on the safe side by making an even higher rate of surplus value than his competitors if possible, he must be constantly on the alert to adopt all available devices for increasing the amount of surplus value that he receives. Marx outlined several of the methods which were at the disposal of the capitalist-employer. Perhaps the most obvious method of increasing surplus value is merely to increase the length of the working day. If the quantity of commodities and services necessary to the subsistence of the worker and his family, and consequently the worker's wage, be taken as fixed, any increase in the length of the working day will increase also the period of uncompensated labor during

<sup>10</sup> *Ibid.*, pp. 176-177.

which the worker is really working to produce surplus value for the employer. Of course, the adding of a couple of hours to an already long working day would probably not increase the surplus value per worker proportionately, but it would increase it to some extent. This method of increasing surplus value was apparently very popular in Marx's day, and he devotes scores of pages to a description of the use of this method and its effects on the workers.

A second method of increasing surplus value is found in the use of machinery. Since machinery itself is incapable of being exploited and can only add its own value to the final products over its life time, it might be considered difficult to see how its use could increase surplus value. Indeed, Marx's notion of the declining rate of profit suggests that heavy investment in machinery and other forms of constant capital tends to lower surplus value at least as a percentage of total capital. This, however, would not keep surplus value per worker, or even total surplus value as an absolute sum, from increasing. The increase in absolute surplus value arises out of the fact that the employer who furnishes his workers with machinery usually requires them to work a longer day than formerly. As Marx said:

Machinery sweeps away every moral and natural restriction on the length of the working day. Hence, too, the economical paradox, that the most powerful instrument for shortening labour time, becomes the most unsailing means for placing every moment of the labourer's time and that of his family, at the disposal of the capitalist for the purpose of expanding the value of his capital.<sup>11</sup>

Since the use of large quantities of machinery tends to reduce the direct labor requirements of the employer, and since the labor-power used is the only source of surplus value, the employer is led to exploit his workers more thoroughly than before.

The use of machinery, and especially the use of new and improved machines and methods of production, may have another effect on surplus value. In many cases, though not by any means in all, such new processes and machines may cut down the cost of producing the commodities and services necessary to the maintenance of the worker and his family. If these commodities and services come to contain less labor-time than formerly, the wage or value of the labor-power also declines. In fewer hours than formerly,

<sup>11</sup> Karl Marx, *Capital*, Volume I, p. 445.

the worker creates enough value to replace his wage and this leaves him more hours per day than formerly to work to create surplus value for the employer, even if the total length of the working day is not increased.

Even if the length of the working day is limited by legal restrictions or otherwise, the employer can increase the surplus value per worker and the total surplus value by speeding up the worker. If the worker comes to turn out more product in a working day of given length and his needs for subsistence do not increase, the amount of surplus value increases. Working harder for a given number of hours is about the same thing as working at the usual rate of speed for a longer period of time. The speeding up of the worker is connected with the use of machinery and of piece-rate wages

So soon as that shortening [of the hours of work] becomes compulsory, machinery becomes in the hands of capital the objective means, systematically employed for squeezing out more labour in a given time. This is effected in two ways by increasing the speed of the machinery, and by giving the workman more machinery to tend<sup>12</sup>

Marx also concluded that

in the workshops under the Factory Acts, piece-wage becomes the general rule, because capital can there only increase the efficacy of the working day by intensifying labour<sup>13</sup>

Finally, the capitalist-employer augments his surplus value by using his workers cooperatively as a team while paying them as if they worked as independent individual labourers. A factory labour force of 100 men working together as a cooperative group will turn out a much greater total product than would the same 100 men working as separate individuals, and yet their individual subsistence needs, and hence their wages, would be no greater. The capitalist-employer does everything he can to promote the efficiency of this cooperative use of labor, and he is not usually criticized for appropriating the extra fruits of the cooperative process. As Marx said

Because this power costs capital nothing, and because, on the other hand, the labourer himself does not develop it before his labour belongs

<sup>12</sup> *Ibid*, p. 450

<sup>13</sup> *Ibid*, p. 609

to capital it appears as a power with which capital is endowed by Nature—a productive power that is immanent in capital.<sup>14</sup>

*The Indictment of Machinery* In general, we see that the Marxian opinion of the development of machinery and its effects on the workers was unfavorable. The use of machinery reduces the proportion of the working day in which the worker is labouring to replace his wage or his subsistence, it leads to a lengthening of the working day, where possible, and it leads to the speeding up of the worker. By decreasing the amount of strength required to do many tasks, the use of machinery makes it possible to employ women and children in industry. They work for very small wages, the wages of men are reduced, and in many cases the total family income is no greater than it was when only the head of the family was employed. Finally, Marx credits machinery with ruining artisans and handicraft producers, displacing workers, and creating a great reserve army of the unemployed. Marx was familiar with the argument of the "vulgar economists" to the effect that technological unemployment is temporary and that, in the long run, technological progress creates as much employment as it destroys, but he did not consider it valid. On the whole, then, Marx paints an extremely gloomy picture. Since wages are fixed at the subsistence level, increases in production, the improved efficiency of industry, and even increases in the productivity of the workers themselves go only to increase the surplus value received by the employers and later shared by them with landowners and pure capitalists.

### *Criticism of the Theory of Surplus Value*

*The Bases of the Theory* In considering the theory of surplus value, we must not forget that this theory is really only a conclusion based on certain premises known as the theory of value and the theory of wages. If we can accept the one premise to the effect that the values of commodities are determined by the quantities of labor-time embodied in them, and the other premise to the effect that wages, or the value of labor-power, being determined in the same fashion, are only enough to provide for the subsistence or maintenance (including training) of the workers and their families, then the theory of surplus value in general terms at least, seems to be valid.

<sup>14</sup> *Ibid.*, pp. 365-366.

On the other hand, if, as we have tried to show, the theories of value and wages themselves are open to most serious objections and cannot be considered valid, the theory of surplus value is left floating around in the air without visible means of support. Clearly, the theory of surplus value can be no stronger than the theories on which it is based, and, if these theories are weak, the existence of surplus value is something that cannot be shown by economic analysis. It must be accepted, if at all, only on faith.

*The Question of Wages of Management* In any case, the theory of surplus value as developed by Marx merits criticism in its own right. We have seen that Marx divided the total income of an enterprise into only two parts—the one necessary to the recapture of the variable capital that has been paid out to the workers as wages, and the other consisting of surplus value which is later divided into rent, interest, and profits. In this simple two-part analysis of the income of an enterprise, one factor seems to be left out of consideration and that is the labor performed by the enterpriser himself and its remuneration. Marx surely would not want to say that there was no socially necessary labor involved in managing a business. The work performed by the business enterpriser is of a different type from that of the ordinary employees, but it is none the less work. Of course, Marx could have escaped any necessity of making provision for the work of management and its remuneration if he had considered the capitalist-employer to be a pure absentee-owner who hired other people to do all the work around the enterprise—the managerial as well as the ordinary labor. However, it is hardly likely that this was Marx's point of view, especially since, in his day, the modern corporation (in which the managers are hired employees and the stock-holders are really a sort of absentee-owners) had not developed to anything like its present importance. Besides, Marx in speaking of the capitalist-employer or enterpriser seems to regard him as the active manager of his business, paying rent to landowners and interest to pure capitalists, and getting his own income out of that segment of surplus value known as "commercial or industrial profits."

If the capitalist-employer is the active manager of his enterprise and if his functions as manager are socially necessary (which seems indisputable), then his labor-time is part of that total labor-time which is responsible for the natural value of the products of the enterprise and his labor-power is deserving of remuneration. Even

on the Marxian basis of evaluating labor-power, the capitalist employer is entitled to receive a wage which is based upon the labor-time necessary to produce or reproduce his labor-power, i.e., a wage which will cover his subsistence and training plus the maintenance of his family. The point is not that we are feeling sorry for the capitalist-employer for not being allowed a wage of management in the Marxian analysis. If he receives as much surplus value as Marx says he does, he is deserving of no sympathy. The point is that any attempt to account for the remuneration of the labor of the capitalist-employer weakens the Marxian analysis of surplus value at one point or another. If the wage for the labor-power of the capitalist-employer is thought of as being included in the surplus value which he receives, then surplus value is no longer a purely unearned income derived from the exploitation of the hapless workers. Instead, part of it is income earned by the capitalist-employer, since it is a payment for his own labor-power. On the other hand, if the wage for the labor-power of the capitalist-employer is thought of as being included in the sum total of wage payments or variable capital, it becomes clear that a part of this variable capital is no longer to be considered as a means of exploiting the workers and a source of surplus value, since we must assume that the capitalist employer is hardly likely to "exploit" his own labor power.

The recognition of the fact that a part of the income of the active capitalist employer must be considered earned, since it is a payment for his own labor-functions in connection with the business, is of considerable importance. The "vulgar economists" of today, for example, think that the capitalist-employer who actively manages his own enterprise and is situated in a competitive industry will be satisfied in the long run if he has left, after paying all expenses of his business, an amount of income which compensates him at a competitive rate for his own functions and services as entrepreneur, and that he does not need to receive any net profit or surplus value (though he will take it if he can get it). The Marxian analysis, on the other hand, seems to suggest that surplus value is the only source of income for the capitalist-employer and that he must therefore exploit his workers in order to survive.

*The Amount of Surplus Value* Whatever else may be said of the Marxian analysis of surplus value, it seems clear that Marx habitually and greatly overestimates the amount of surplus-value which it is possible for the capitalist employers to receive. The Marxian

illustrations of surplus value suggest that it is the usual thing for the capitalist-employers, by paying out a certain amount of variable capital as wages, to receive a total income which is double the amount of variable capital paid out. In other words, the total amount of surplus value is just about equal to the wage bill or the total of wage payments. In actual practice, many studies which have been made for leading capitalistic countries, such as the United States and England, indicate that wages and salaries amount to around two-thirds of the total national income (and in individual fields of economic activity amount to 75 or even 85 per cent of total income produced). Even if all other income than wages and salaries were considered to be unearned income or surplus value, it would obviously be completely impossible for surplus value to be anything like as great as the total of wage and salary payments in such cases. Whether we approve or disapprove of rent, interest, and profits, these incomes combined are not nearly so large a segment of the national income as that which goes into wages and salaries.

*The Significance of Machinery* It also seems clear from the analysis of surplus value and of the methods of increasing it that Marx greatly misunderstood the significance of machinery and its effects on the economic status of the workers. There can be no doubt, of course, that unscrupulous employers, figuring that work with machinery is considerably lighter than the same kind of work without machinery, have lengthened the working day and speeded up the workers. On the other hand, although Marx thought he saw a tendency for the working day to lengthen as the use of machinery developed, it cannot be denied that the average working day in capitalistic systems at the present time is far shorter than it was in Marx's day. While workers are sometimes speeded up unduly, in general it may be thought that they are willing to work hard during a short working day in order to enjoy more leisure time and that their intensified efforts have found recognition in higher wages and real incomes. The use of machinery has led undoubtedly to the increased employment of women and children and these employees at times have been mercilessly exploited by means of low wages, long hours, and inhuman working conditions. On the other hand, the employment of women and children has more often been a result of poverty than an important cause of it and has often been used as the means of obtaining a better family income than was formerly received. The notion that, when women and children

work, the family income tends to fall to the previous wage of the man working alone seems to have little foundation in fact We are not arguing, of course, for the employment of child labor, for the use of child labor is ordinarily to be considered undesirable, but, as far as the labor of women goes, there is no doubt that it has increased the total national output of goods and services, or national income, and that it has increased the total amount of income going to the workers and their families as a whole It would seem ridiculous to argue that our national income would be as great as it now is, if all women were excluded from employment In connection with all of these matters, Marx seems to have underestimated the significance and importance of such things as protective social legislation, organizations of workers, public opinion, the shift system, and the discovery that, in many lines of production, the worker can accomplish as much in the long run in a relatively short day as in a relatively long one-

The problem of technological unemployment, which Marx noted, is an important one The individual workers who are displaced by labor-saving machinery seldom remain unemployed for long periods of time, but, from the point of view of the economy as a whole, the problem of technological unemployment is a continuous one And it becomes even more serious than usual when the technological changes which cause it are rather general throughout the economy and when workers are displaced by machines during periods of general business depression Although a great deal of misery and suffering may result from rapid technological change, we must in general agree with the "vulgar economists" who say that the long-run effect of technological change is to increase the real incomes and standards of living of everyone without in any way decreasing the total amount of employment available for labor With human wants for economic goods rapidly growing and indefinitely expandible, there is no likelihood that we shall learn to produce everything so efficiently that the total of work which needs to be done will be inadequate to provide jobs for all of our workers And, even in the short run, we provide for our unemployed workers on a scale which Marx would probably have deemed incredible It seems impossible today to agree with Marx's general conclusion that machines are the enemy of the toiling masses of workers

*The Declining Rate of Profit* We now turn again to the concept of the declining rate of profit, or Marx's notion that the rate of

profit achieved by an enterprise would decline as the enterprise increased in size and invested a greater proportion of its total capital in constant capital rather than variable capital. This concept, it will be remembered, resulted from Marx's distinction between the rate of profit and the rate of surplus value, his distinction between constant and variable capital, and his idea that only variable capital, or funds invested in the payment of wages to workers, can be productive of surplus value. It is rather easy to illustrate the declining rate of profit. Let us consider three hypothetical firms, A, B, and C, all with the same amount of variable capital but with varying amounts of constant capital. To simplify matters, suppose that all three firms advance or turn over their capital once each year, that all their products are sold at the end of the year, and that they employ the same number of workers at the same wage rate. The situation is then as follows:

Firm	Constant	Capital Variable	Total	Surplus Value	Rate of Surplus Value	Rate of Profit
A	\$ 5,000	\$5,000	\$10,000	\$5,000	100%	50%
B	15,000	5,000	20,000	5,000	100%	25%
C	25,000	5,000	30,000	5,000	100%	16 7%

It is clear in this simplified example that the absolute amount of surplus value and the rate of surplus value is the same from firm to firm but that the rate of profit declines from 50 per cent to 25 and 16 7 per cent as we pass from the smallest to the largest firm.<sup>15</sup> Moreover, the same conclusion would be reached even if the absolute amount of variable capital and of surplus value increased moderately from the smallest firm to the largest firm. That is, if Firm C found it necessary to pay out \$10,000 of variable capital in wages, along with its \$25,000 of constant capital, and received a surplus value of \$10,000, the rate of surplus value would be 100 per cent but the rate of profit would be only 28 57 per cent or less than that of Firm A.

The concept of the declining rate of profit left Marx with some things to explain. In the first place, if the rate of profit tends to decline as a firm increases its size and invests a greater proportion of its total capital in constant capital, in spite of the fact that the absolute amount of surplus value remains constant or increases

<sup>15</sup> This illustration is adapted from Karl Kautsky, *The Economic Doctrines of Karl Marx*, pp. 84-88.

actually, and if the enterprise regards this result as a calamity, why does he attempt to increase the size of his firm and why does he invest more and more heavily in constant capital? If we disregarded the typical numerical illustration which we have given, it would seem possible to answer this question within the Marxian analysis. That is, any one firm would have an incentive to grow and use large amounts of new machinery because it would expect to make more money by doing so. As it adopted new machines and labor saving devices, it would produce each unit of product with a smaller expenditure of labor-time than formerly, but the labor-time spent on the product on the average throughout the industry would not yet have declined. Consequently, our one firm would receive the same price as usual for its product but would have smaller cost per unit of product than formerly, and hence would gain. Then after the new type and scale of machinery had been adopted by a number of firms, the average amount of labor-time embodied in the product would be reduced, and the remaining firms would be compelled to undergo the same development. If they failed to do so, they would have the same cost in terms of labor-time per unit of product as formerly and would get a lower price per unit of product than formerly, and would be in danger of being eliminated from the competitive struggle. In this way all the firms would become larger in the long run without any firm having a permanent differential gain in terms of profit.

This explanation is, of course, quite inconsistent with the usual numerical illustration (since this type of illustration indicates that a firm's wage bill remains as large as ever as it increases its constant capital and that its absolute profit is no greater than before) and Marx did not rely on it. In fact, Marx was concerned not so much with any purely theoretical discrepancies as with the fact that his declining rate of profit was apparently in conflict with reality. That is, he thought he saw that large-scale firms with heavy investments in machinery and in constant capital in general were no worse off with respect to the rate of profit than small firms with a much smaller proportion of their total capital invested in constant capital. It is very difficult to test the present accuracy of his observation in this matter. One recent study of the relative profitability of large and small corporations in the United States, defining profits as the ratio of net income to net worth, found that the large corporations

that made profits made them at lower rates than the small ones in the period 1931-33, while the large corporations that lost money lost at lower rates than the small ones

In 1933, the profitable corporations in the smallest class (those with assets of \$50,000 or less) made an average profit of 8.6 per cent while profitable corporations in the largest class (those with assets of \$50,000,000 or more) made an average profit of only 4.7 per cent. However, unprofitable corporations in the smallest class had an average loss of 37.8 per cent against a loss of only 2 per cent on the average for unprofitable corporations in the largest class. The only group of corporations that had a profit on the average in each year was the largest, though only a minority of the 594 giant corporations made money.<sup>16</sup> This study, then, does not make the average position of the large firms with respect to profits look particularly unfavorable. On the other hand, some studies that have been made of the earnings of large combinations of business units in the United States have concluded that in most cases these combinations have not been able to make earnings as great, as a percentage of investment, as those formerly enjoyed by the individual firms which went into the combinations.

Even if large firms did tend to make profits at a lower rate on their total investment than small firms, this result would not necessarily be considered particularly unfavorable from the point of view of the large firms. It is quite possible to see why a firm would prefer to make a profit of \$50,000 on a total investment of \$300,000 than to make \$25,000 on a total investment of \$100,000, even though the rate of profit would be lower in the former case. And this preference might be particularly strong if the earnings on the larger investment would be more stable through time than those on the smaller investment. However, Marx thought that the rate of profit was just as favorable for large concerns with relatively large investments in constant capital as for small firms with relatively small investments in constant capital, and he was much concerned over this discovery since it seemed to contradict his theory that the expenditure of variable capital in paying wages was the only source of surplus value and profit.

Thus, Marx said

<sup>16</sup> *How Profitable Is Big Business?* New York: The Twentieth Century Fund, 1937, pp. 145-146.

The rate of surplus value, or the degree of exploitation of labour-power, and the value of labour-power, or the amount of necessary working time being given, it is self evident that the greater the variable capital, the greater would be the mass of value produced and of the surplus value. With a given rate of surplus value, and a given value of the labour-power, therefore, the masses of surplus value produced vary directly as the amounts of variable capital advanced. This law clearly contradicts all experiences based on appearance. Everyone knows that a cotton spinner, who, reckoning the percentage on the whole of his applied capital, employs much constant and little variable capital, does not, on account of this, pocket less profit or surplus value than a baker, who relatively sets in motion much variable and little constant capital. For the solution of this apparent contradiction, many intermediate terms are yet wanted, as from the standpoint of elementary algebra many intermediate terms are wanted to understand that  $\frac{0}{0}$  may represent an actual magnitude.<sup>17</sup>

Marx did not propose any solution to this problem in Volume I or Volume II of his *Capital*, but when he did get around to suggest a solution in Volume III, it proved to be a revolutionary one indeed. As Marx put it

Now if the commodities are sold at their values, then, as we have shown, considerably different rates of profit arise in the various spheres of production, according to the different organic composition of the masses of capital invested in them. But capital withdraws from spheres with low rates of profit and invades others which yield a higher rate. By means of this incessant emigration and immigration, in one word, by its distribution among the various spheres in accordance with a rise in the rate of profit here, and its fall there, it brings about such a proportion of supply to demand that the average profit in the various spheres of production becomes the same, so that values are converted into prices of production.<sup>18</sup>

Let us see what this would mean in terms of the three firms which we previously examined. These firms are still of different sizes and they still have different organic compositions of capital, or different proportions of constant and variable capital. However, in the new long-run equilibrium which Marx is describing, they are making equal rates of profit.

<sup>17</sup> Karl Marx, *Capital*, Volume I, pp. 334-335

<sup>18</sup> Karl Marx, *Capital*, Volume III, p. 230

Firm	<i>Capital</i>			<i>Surplus Value Produced</i>	<i>Rate of Surplus Value</i>	<i>Rate of Profit</i>	
	<i>Constant</i>	<i>Variable</i>	<i>Total</i>			<i>Profit</i>	<i>Profit</i>
A	\$ 5,000	\$5,000	\$10,000	\$5,000	100%	\$2,500	25%
B	15,000	5,000	20,000	5,000	100%	5,000	25%
C	25,000	5,000	30,000	5,000	100%	7,500	25%

This curious result, the equalization of the rate of profit, comes about because of the fact that commodity prices deviate now from commodity values. Profit, as it were, becomes added into total costs and the result, on a per-unit basis, is production price. The actual prices of individual commodities vary now around production prices instead of around value in terms of labor-time.<sup>19</sup> Putting it another way, the surplus value produced by each firm still depends upon and is proportional to variable capital, but each firm no longer receives the amount of surplus value which it is responsible for creating. Instead, in the process of marketing the products, all the surplus value goes into what might be called a kind of common pool, from which it is withdrawn by the individual firms not in proportion to their variable capital but in proportion to their total capital. This result occurs because the exchange-value which each firm is able to command for its product depends now on production price, or average total costs of all kinds, rather than on costs in terms of labor-time.

This explanation is helpful in showing how firms of different sizes, with different organic compositions of capital, and even producing different types of products, can make net earnings or profits at the same rate. However, the explanation does violence to some of Marx's most important theories. Though surplus value is "produced" by variable capital only, this fact loses significance now that surplus value is "received" on the basis of total capital. For all practical purposes, a firm is just as likely to obtain surplus value by using large amounts of constant capital as by using large amounts of variable capital. This, of course, is inconsistent with the former Marxian idea that a firm derives its surplus value only from the variable capital which it employs. Again, the only way in which the firms can draw surplus value out of the "pool" on the basis of total capital is to have the exchange-value of the final products depend upon total costs, and not merely on labor costs or expenditures of

<sup>19</sup> Karl Kautsky, *The Economic Doctrines of Karl Marx*, pp. 81-8.

variable capital This conclusion contradicts the regular Marxian theory of value which makes exchange-value depend on labor-time and not on costs of production

Marx was well aware that this new explanation of his was inconsistent with his regular analyses of value and surplus value, but, while he struggled manfully to do so, he was unable to bring about a reconciliation of the divergent explanations As one critic says

In hundreds of pages of *Capital*, Volume III, with endless repetition and futile effort to escape from his own net, he is forced to the conclusion that prices are not proportional to variable capital or labor cost, and that rates of profit are in no wise related to rates of surplus value In dialectical terms, the labor cost theory, carried to its logical conclusion, brought about its own negation<sup>20</sup>

In the end, in an effort to salvage something of his theory of value, Marx contended that the sum of all the prices of production of all commodities in society, comprising the totality of all lines of production, is equal to the sum of all the values [based on labor-time] But this contention, even if true, would not reconcile the exchange-values or production prices of individual commodities with their "values" based on labor-time

#### QUESTIONS

- 1 What were the assumptions on which the Marxian theory of surplus value was based?
- 2 Explain the Marxian theory of surplus value briefly
- 3 "Marx clearly intimates that the creation of surplus value is an inevitable characteristic of a capitalistic economic system" Explain
- 4 "Surplus value, according to Marx, does not result from selling the products of labor for more than they are worth or from paying the workers less than their labor power is worth" Show whether you agree
- 5 Distinguish between constant and variable capital What is the significance of this distinction in connection with the theory of surplus value?
- 6 Distinguish between the rate of surplus value and the rate of profit Why did Marx think the rate of profit tended to decline under capitalism?
- 7 How, according to Marx, does the capitalist employer attempt to increase the amount of surplus value produced by his workers? Explain

<sup>20</sup> J. L. LeRossignol, *From Marx to Stalin*, p. 206 Reprinted by permission of the Thomas Y. Crowell Company, New York.

- 8 "The Marxian theory of surplus value can be no stronger than the Marxian theories of value and wages" Explain
- 9 "The Marxian theory of surplus value follows logically enough from the theories of value and wages, but it is nevertheless open to several grave objections" Explain
- 10 Show how the Marxian theory of surplus value is strengthened or weakened according to the way in which the "subsistence of the workers" is interpreted
- 11 "One weakness of the theory of surplus value is found in the fact that it makes no allowance for the productive services of business enterprisers and the remuneration of these services" Explain
- 12 "Marx habitually and greatly overestimated the amount of surplus value which it was possible for the capitalist employers to receive" Show whether you agree
- 13 "Marx greatly misunderstood the significance of machinery and its effects on the economic status of the workers" Do you agree? Explain
- 14 Criticize the Marxian theory of the declining rate of profit
- 15 "In view of his theory of the declining rate of profit, Marx had great difficulty in explaining why firms with relatively large proportions of constant capital sometimes achieve higher rates of profits than other firms" Explain
- 16 "When Marx got around to explain why firms with relatively large proportions of constant capital make rates of profit which are as satisfactory as those of other firms, his explanation did violence to some of his other theories" Explain
- 17 "It is quite possible that, if Marx were writing today with the assistance of modern value theory, he would establish quite a different theoretical basis for his surplus value or exploitation thesis" What bases could be found in the operation of modern capitalism for a surplus value or exploitation thesis? Explain

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## CHAPTER 29

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### THE MARXIAN PREDICTIONS CONCERNING CAPITALISM

On the basis of his analysis of the way in which the capitalistic system was operating in his day (as contained in the theories of value, wages, and surplus value) and his interpretation of the general manner in which history-making forces operate, Marx undertook to make a number of predictions concerning the future operation of the capitalistic system and its eventual fate. These predictions boded no good for the hated capitalistic system. The Marxian predictions deserve and will receive a fairly detailed analysis, but we shall first attempt a general sketch or outline of them.

*The Predictions Summarized.* Marx predicted that the future operation of capitalism would be marked by a succession of business cycles and depressions of ever increasing severity. These partial breakdowns of capitalism depended upon a conflict between the rapidly expanding productive power of the capitalistic system and its antithesis, the extremely limited consuming power of the toiling masses with their subsistence incomes. As the business cycles ran their unceasing round, the ownership of capital would be concentrated in the hands of an ever dwindling number of large members of the bourgeoisie. On the other hand, the proletariat would become increasingly miserable. This result would follow in part from the fact that the workers were tied to subsistence wages in the face of the ever increasing efficiency, productivity, wealth, and income of the system as a whole. Again, it would result from increased unemployment and the development of a growing labor reserve. As capital became concentrated in fewer and fewer hands and as the proportion of constant capital to total capital increased, the labor requirements of the capitalistic system would decline and large numbers of persons would be unable to find work. Here then

is another conflict or contradiction between the growing wealth and affluence of the bourgeoisie and the increasing misery of the proletariat.

Eventually, conditions of monopoly would be present in almost every field of production, and there would be an unholy alliance between the few remaining industrialists and powerful banking and financial interests. The dwindling number of exploiters would become increasingly dissatisfied with the domestic operation of the capitalistic economy and would reach out to secure foreign markets. In attempting to insure and protect these markets, a policy of imperialism with respect to backward areas would be followed with the assistance of the bourgeois-controlled state. In this international field, there would be conflicts of interest between different capitalistic economies, all in search of markets, and severe wars would be fought between the nations. In the end, the capitalistic system would break down and collapse in the middle of a severe depression or a cataclysmic war. At this juncture, the members of the downtrodden proletariat would rise up, throw off their chains, stage a revolution, and take over the operation of the state, government, and economic system. The capitalistic system, which began to die on the day when it was born, would at long last have met its demise. Or as Marx would say, the capitalistic system would have achieved, with the inexorability of a law of nature, its own negation.

### *The Increasing Severity of Business Cycles*

**The Theory of Business Cycles** The general Marxian theory of the business cycle is that known as the underconsumption (or over-production) theory. There is a great conflict between the enormous productive powers generated by the capitalistic system and its limited powers of consumption based on subsistence wages for the toiling masses. The great industries of capitalism inevitably engage in large-scale or mass production of goods of such kinds as must be consumed, if at all, by the great masses of workers while on the other hand the distribution of income is such that these workers cannot purchase, at prices equal to their natural values, the economic goods which have been produced for them. The workers, since they are paid in wages only a part of the values of the commodities which they create, cannot turn around and purchase all these commodities at their full values based upon the amount of

labor time embodied in them Capitalistic distribution of income is in conflict with capitalistic production

In Marx's own words

The last cause of all real crises always remains the poverty and restricted consumption of the masses as compared to the tendency of capitalistic production to develop the productive forces in such a way that only the absolute power of consumption of the entire society would be their limit<sup>1</sup>

Again,

The conditions of direct exploitation and those of the realization of surplus value are not identical They are separated logically as well as by time and space The first are only limited by the productive power of society, the last by the proportional relations of the various lines of production and by the consuming power of society The last-named power is not determined either by the absolute productive power nor by the absolute consuming power, but by the consuming power based on antagonistic conditions of distribution, which reduces the consumption of the great mass of the population to a variable minimum within more or less narrow limits<sup>2</sup>

And again

The stupendous productive power developing under the capitalist mode of production and the increase, though not in the same proportion, of capital values (not their material substance), which grow much more rapidly than the population, contradict the basis, which, compared to the expanding wealth is ever narrowing and for which this immense productive power works, and the conditions, under which capital augments its value This is the cause of crises<sup>3</sup>

Thus, briefly stated, it is Marx's conclusion that

the contradictions between the striving of capital to achieve a limitless expansion of production, so as to receive as big profits as possible, and the narrow bounds of the consuming power of capitalist society which are conditioned primarily by the low material standards of the masses of the working people, lead inevitably to crises of overproduction<sup>4</sup>

<sup>1</sup> Karl Marx, *Capital*, Volume III, p. 568

<sup>2</sup> *Ibid.*, p. 286

<sup>3</sup> *Ibid.*, pp. 312-313

<sup>4</sup> E. Varga, "The New World Economic Crisis in the Communist International," January, 1938, p. 22

However, this is another of the many points on which Marx had more than one opinion. He seems to deny his own general theory when he says

It is purely a tautology to say that crises are caused by the scarcity of solvent consumers, or of a paying consumption. But if one were to attempt to clothe this tautology with a semblance of a profounder justification by saying that the working class receive too small a portion of their own product, and the evil would be remedied by giving them a larger share of it, or raising their wages, we should reply that crises are precisely always preceded by a period in which wages rise generally and the working class actually get a larger share of the annual product intended for consumption.<sup>5</sup>

Marx also indicated that he was using the term "overproduction" in a limited and relative sense. As he said

It is not a fact that too many necessities of life are produced in proportion to the existing population. The reverse is true. Not enough is produced to satisfy the wants of the great mass decently and humanely. It is not a fact that too many means of production are produced to employ the able-bodied portion of the population. The reverse is the case. In the first place, too large a portion of the population is produced consisting of people who are really not capable of working, who are dependent through force of circumstance on the exploitation of the labor of others or compelled to perform certain kinds of labor which can be dignified with this name only under a miserable mode of production. In the second place, not enough means of production are produced to permit the employment of the entire able-bodied population under the most productive conditions, so that their absolute labor time would be shortened by the mass and effectiveness of the constant capital employed during working hours.

On the other hand, there is periodically a production of too many means of production and necessities of life to permit of their serving as means for the exploitation of the laborers at a certain rate of profit. Too many commodities are produced to permit of a realisation of the value and surplus-value contained in them under the conditions of distribution and consumption peculiar to capitalist production, that is, too many to permit of the continuation of this process without ever recurring explosions. It is not a fact that too much wealth is produced. But it is true that there is periodical over-production of wealth in its capitalistic and self-contradictory form.<sup>6</sup>

*Increasing Severity* Business cycles are not only bound to occur in the operation of a capitalistic system but they tend to become in-

<sup>5</sup> Karl Marx, *Capital*, Volume II, p. 475

<sup>6</sup> Karl Marx, *Capital*, Volume III, pp. 302-303

creasingly severe as time goes on. After each depression, there are fewer surviving capitalist employers and the productive wealth of the system is concentrated in fewer hands. Competition is keen and the surviving capitalist employers, in their quest for productive efficiency, invest ever larger proportions of their growing individual capitals in machinery and other forms of constant capital. On the other hand, this same development sharply limits the direct labor requirements of the firms, and, while relatively few workers are employed, their wages are still tied to the subsistence level. Therefore, the forces which cause the productive power of the capitalistic system to increase from cycle to cycle also cause the workers, with their subsistence incomes, to be ever more completely unable to take from the market, at prices which will give the capitalist employers the rates of surplus value and profit which they expect, the commodities which capitalistic industries are able to produce. The conflict between increasing productive power and limited effective consuming power grows worse and worse, and each business cycle brings the capitalistic system nearer to its eventual doom.

*The Validity of the Prediction.* In evaluating Marx's attitude on the subject of business cycles, we shall not be primarily concerned with the underconsumption overproduction theory as such, for a complete analysis of this theory would take us far afield. However, we may say that, in general, the attempt to find a single factor explanation of the business cycle is as unfortunate as the attempt to find a single-factor explanation of the values of commodities. Even those economists who detect an element of truth in the Marxian explanation of the business cycle would not be likely to claim that it is a sufficient and adequate theory. Whatever may be the division of income as between the workers on the one hand and landowners, capitalists, and enterprisers on the other, there would seem to be no reason why capitalistic production could not be adjusted to turn out the right goods in the right quantities for every class of income-receivers. Enterprisers certainly do not aim to produce goods that cannot be taken off the market by the people for whom they are produced, and, if this result seems to occur from time to time, it should be attributed perhaps to the anarchy of capitalistic production and errors in forecasting effective demand in the market rather than to an insufficiency of purchasing power on the part of the workers. Even if it were possible to agree with Marx that the insufficiency of the workers' purchasing power is the cause of de-

pressed business conditions, it is difficult to see why this factor by itself should cause business to run in cycles of boom and depression. If the workers, year in and year out, receive in wages only a fraction of the values which they create and if the commodities which they produce are of such a kind that they must be sold back to the workers if they are to be sold at all, we may see that the result would be relative overproduction or underconsumption and depressed business conditions, but such a state of depression should apparently be constant and permanent rather than recurring. Since the workers are always incapable of buying the goods which are produced for them, it is difficult to see just what would cause depression to turn into a new boom period every so often. These and many other objections may be raised concerning Marx's theory of business cycles.

Again, we are not going to argue whether Marx was right in saying that business cycles, regardless of specific causes, are inevitable under capitalism, for it would seem that a rather good argument could be made out for this point of view. Our chief concern is with the validity of the proposition that business cycles in the capitalistic system tend to become increasingly severe as time goes on. Has this prediction actually proved to be valid? If we take the prediction to mean that business cycles would become more severe in an absolute sense, we must admit the validity of the prediction. There can be little doubt that the great business cycles of today are bigger and better than those of many years ago. However, this result was almost completely automatic and unavoidable. If, under normal conditions today, our large economy has a much larger number of enterprises, a larger number of workers, and a greater total of physical production than it had many years ago, it would be expected that, when a depression came along, there would be more business failures, more unemployed workers, and a greater slump in physical production than occurred in the depressions of many years ago.

If, however, we change the question and ask whether business depressions are relatively more severe today than they were years ago, the answer is not nearly so obvious. If in ordinary times today we have a working force of 45,000,000 workers and 15,000,000 of these workers become unemployed in a great depression, unemployment is relatively no more severe than in an earlier depression in which it reached, for example, 4,000,000 workers on the basis of

a normal labor force of 12,000,000 workers To have 5000 banks fail out of 20,000 is relatively no worse than to have 1000 banks fail out of 4000, and so on In other words, if we always related the magnitude of depression events to the bases from which they started, we could not be sure of finding that modern depressions are more severe than those of Marx's time Many people today, basing their opinion largely on their vivid recollections of the great depression after 1929, would be willing to argue that modern business cycles are both relatively and absolutely more severe than those of many years ago, but if we go back to read the things which people wrote about the severe depressions of 1837 or 1873, for instance, we get the impression that the cycles of those days seemed as severe to those who experienced them as modern cycles seem to us

Whether or not the prediction with regard to the increased severity of the business cycle is regarded as having come true, it may well be that the prediction had considerable *prospective* validity as of the time when Marx was forming his opinions Before the Industrial Revolution, business cycles in the modern sense hardly existed There were undoubtedly weather cycles and crop cycles, and people in general were probably better off in some years than in others, but business cycles as such could hardly be of much importance until the system of roundabout, large-scale, specialized production with its dependence on the complicated exchange and credit mechanism had developed Marx, on the basis of his studies of economic conditions as they had existed in the relatively uncomplicated times before the development of modern capitalism, could hardly have remained unimpressed by the recurring depressions of 1837, 1847, 1857, 1866, and 1873 which he observed And he may perhaps be forgiven for thinking that business cycles, if they were not already becoming more severe, would certainly do so in the future

### *The Concentration and Centralization of Capital*

***The Concentration of Capital*** Another Marxian prediction concerning the future of capitalism had to do with the concentration and centralization of capital The concentration of capital referred only to the tendency for capital as a whole to accumulate Starting with the primitive accumulation of capital through expropriation,

the capitalist-employers have always converted a large part of their surplus value into more capital. In turn, more capital meant the ability to employ more workers, more exploitation, more surplus value, more capital, and so on and on. Capital thus tended to increase in total size like a snowball rolling down hill, and Marx predicted that the accumulation of capital under capitalism would continue far into the future. In this part of the prediction, there was no reference to the concentration of the growing stock of capital in the hands of fewer and fewer capitalist-employers, although some people do find in it the notion that, in the future, additions to the total stock of capital will probably pass primarily into the hands of the capitalist-employers who are already largest.

In speaking of the simple accumulation or concentration of capital, Marx said:

A certain accumulation of capital, in the hands of individual producers of commodities, forms therefore the necessary preliminary of the specifically capitalistic mode of production. We had, therefore, to assume that this occurs during the transition from handicraft to capitalistic industry. It may be called primitive accumulation, because it is the historic basis, instead of the historic result of specifically capitalist production. How it itself originates, we need not here inquire as yet. It is enough that it forms the starting point. But all methods for raising the social productive power of labour that are developed on this basis, are at the same times methods for the increased production of surplus-value or surplus-product, which in its turn is the formative element of accumulation. They are, therefore, at the same time methods of the production of capital by capital, or methods of its accelerated accumulation. The continual retransformation of surplus value into capital now appears in the shape of the increasing magnitude of the capital that enters into the process of production. This in turn is the basis of an extended scale of production, of the methods for raising the productive power of labour that accompany it, and of accelerated production of surplus value. If, therefore, a certain degree of accumulation of capital appears as a condition of the specifically capitalist mode of production, the latter causes conversely an accelerated accumulation of capital. With the accumulation of capital, therefore, the specifically capitalistic mode of production develops, and with the capitalist mode of production the accumulation of capital. Both these economic factors bring about, in the compound ratio of the impulses they reciprocally give one another, that change in the technical composition of capital by which the variable constituent becomes always smaller and smaller as compared with the constant. Two points characterize this kind of concentration which grows directly out of, or rather is identical with, accumulation. First, The increasing concentration [ac-]

cumulation] of the social means of production in the hands of individual capitalists is, other things remaining equal, limited by the degree of increase of social wealth Second The part of social capital domiciled in each particular sphere of production is divided among many capitalists who face one another as independent commodity producers competing with each other?

But this is only a part of the process of capital development The other part is found in the centralization of capital or the tendency for already existing capital, without regard for its accumulation, to become concentrated in the hands of a smaller and smaller number of larger and larger capitalists As Marx says

It is concentration of capitals already formed, destruction of their individual independence, expropriation of capitalist by capitalist, transformation of many small into few large capitals This process differs from the former in this, that it only presupposes a change in the distribution of capital already to hand, and luminously, its field of action is therefore not limited by the absolute growth of social wealth, by the absolute limits of accumulation Capital grows in one place to a huge mass in a single hand, because it has in another place been lost by many This is centralisation proper, as distinct from accumulation and concentration

The laws of this centralisation of capitals, or of the attraction of capital by capital, cannot be developed here A brief hint at a few facts must suffice The battle of competition is fought by cheapening of commodities The cheapness of commodities depends, *caeteris paribus*, on the productiveness of labour, and this again on the scale of production Therefore, the larger capitals beat the smaller It will further be remembered that, with the development of the capitalist mode of production, there is an increase in the minimum amount of individual capital necessary to carry on a business under its normal conditions The smaller capitals, therefore, crowd into spheres of production which Modern Industry has only sporadically or incompletely got hold of Here competition rages in direct proportion to the number, and in inverse proportion to the magnitudes, of the antagonistic capitals It always ends in the ruin of many small capitalists, whose capitals partly pass into the hands of their conquerors, partly vanish Apart from this, with capitalist production an altogether new force comes into play—the credit system

In its beginnings, the credit system sneaks in as a modest helper of accumulation and draws by invisible threads the money resources scattered all over the surface of society into the hands of individual or associated capitalists But soon it becomes a new and formidable weapon in the competitive struggle, and finally it transforms itself into an immense social mechanism for the centralisation of capital Competition and credit, the two most powerful levers of competition develop in propor-

<sup>7</sup> Karl Marx, *Capital*, Volume I, pp 684 686

tion as capitalist production and accumulation do. Nowadays, then, the mutual attraction of individual capitals and the tendency to centralisation are stronger than ever before.<sup>8</sup>

The process by means of which the larger capitals beat the smaller and one capitalist kills many also apparently is closely connected with the recurrence of business depressions. In each depression, the smaller and weaker capitals are unable to stand the strain and fall by the wayside. The smaller capitalists may, in some cases, become co-partners of the larger capitalists aiding in the work of management and sharing in the profits, but more commonly they sink into the proletariat and degenerate into paid workers. When the depression is over, the surviving capitalist-employers continue their intense competition. They strive to increase efficiency and cheapen their commodities, but this requires a more extensive use of machinery and an increase in the proportion of constant capital in their businesses. This, in turn, leads to a reduction in their direct labor requirements and has an unfortunate effect on the total income and consuming power of the toiling masses. The capitalist-employers are unable to sell their products at prices which will produce the rates of surplus value and profit that had been expected on the basis of the labor-time put in by the workers in relation to the labor-time required to produce their subsistence. A new depression based on relative overproduction and underconsumption appears and once more the smaller of the remaining capitalist-employers are eliminated. Their capitals are partly absorbed by the remaining capitalist-employers and partly vanish. After the depression is over, the surviving capitalist-employers stage the same show all over again, and so on and on, until only monopolies survive.

*The Validity of the Prediction.* Have the Marxian predictions with regard to capital development proved to be valid? In other words, if Marx were alive today, would he be satisfied with the present degree of accumulation and centralization of capital in the United States as an indication that his predictions with respect to capital development had come true? It is our impression that Marx would not be at all displeased with what he would find in the United States today. Certainly the accumulation of capital has gone on rather steadily since Marx's day and the present social stock of

<sup>8</sup> *Ibid.*, pp. 686-687.

capital is far greater than that which existed in the 1880's. It might also be argued that additions to the total stock of capital are now made and owned primarily by the larger firms in view of the fact that in 1937 the American corporations with assets of \$1,000,000 or more were responsible for 88 per cent of the total savings of all corporations in the nonfinancial group, though they made up only 5 per cent of the total number of these corporations.<sup>9</sup>

The evidence on the question of centralization of capital is also in favor of Marx's prediction in a general way. As we have seen, corporations transact around two-thirds of the total volume of business in the United States, and own nearly 80 per cent of all business wealth. The ownership of corporate wealth is highly concentrated. In 1937, corporations with assets of less than \$50,000 each made up 55 per cent of all corporations by number but owned only 15 per cent of total corporate assets. On the other hand, the 394 largest corporations owned about 45 per cent of all corporate assets, though they made up less than 0.1 per cent of the total number of corporations.<sup>10</sup> There were some 30 "billion-dollar" corporations in the United States. Each of the largest two of these corporations had larger total assets than any of 38 of our 48 states, and the smallest of the 30 corporations had total assets greater than any one of 18 of our states.<sup>11</sup> In 1936, the 200 largest nonfinancial corporations had total assets of over \$75,000,000,000, or something like one-fourth of the national wealth.<sup>12</sup> In 1937, the corporations which had net incomes of less than \$5000 received less than 2 per cent of the total income of all corporations filing income tax-returns, though they made up 65 per cent of the total number of these corporations. On the other hand, 248 corporations at the top of the heap received 40 per cent of the total net income of all corporations, though they made up only 0.1 per cent of the total number of corporations with incomes.<sup>13</sup>

It is often contended, of course, that this great concentration of productive wealth and income in the hands of a small number of

<sup>9</sup> Temporary National Economic Committee, *Final Statement of Senator Joseph C O'Mahoney*, p. 9

<sup>10</sup> *Ibid.*, p. 7

<sup>11</sup> *Ibid.*, p. 5

<sup>12</sup> National Resources Committee, *The Structure of the American Economy* Washington, Government Printing Office, 1939, pp. 274-276

<sup>13</sup> Temporary National Economic Committee, *Final Statement of Senator Joseph C O'Mahoney*, p. 8

large firms is not very significant because the corporations themselves are widely owned. The ownership of corporate stocks is widespread, and it is well known that many large corporations have many thousands, or even hundreds of thousands, of stockholders. On the other hand, while many people own stocks in corporations, it seems that relatively few people own large numbers of shares, for it is estimated that one-half of all dividends paid in the United States are received by stockholders who comprise less than 1 percent of all American corporate stockholders. In any event, it is clear enough that in the case of our corporations the question of ownership is not nearly so important as that of control, and most of the corporations, however widely they may be owned, are controlled by a very small number of individuals. The simple fact is that most holders of corporate stocks have virtually nothing to do with the control or management of the businesses and are pure absentee-owners. The large corporations, besides being controlled individually by a small number of people, are connected with each other in many cases through interlocking directorates or through dealing with the same investment banking house, or in other ways. Some members, at least, of the controlling group of one large corporation are likely to be members of the controlling groups of other large corporations.

The concentration and centralization of capital has not come about in the manner which Marx prescribed. Only a confirmed Marxian could see in the great accumulation of capital which has occurred in the United States over the past century nothing more than the plowing back into capital of great amounts of surplus value derived from the exploitation of the workers. With regard to the centralization of capital, it is certain that Marx meant centralization of ownership, for the corporation as a form of business organization has developed largely, though not entirely, since his time. While Marx could not foresee the part that corporations would play in modern economic life, there is little reason to think that he would be dissatisfied with modern concentration of the control over capital as a substitute for his predicted concentration of ownership. On the other hand, it may be admitted that the rather widespread ownership of wealth and capital affords our capitalistic system some protection against revolutionary tendencies. Capital has accumulated in our system to an extent that would probably satisfy Marx, but the centralization of capital has not yet become so great.

as he predicted. That is, it has not reached the point at which each industry or business is dominated by a monopoly, though there are some people who would agree that we are rapidly getting to that point.

We cannot be sure just on what basis Marx made his predictions concerning the concentration and centralization of capital. They may have been based in part on his observation of economic development in England and other capitalistic countries. In the early decades of modern capitalism (after the Industrial Revolution), business enterprisers comprised the relatively scarce productive factor and thousands of individuals rushed in to become enterprisers, with the result that most of them failed to survive, though industry and business as a whole managed to grow rapidly. On the other hand, there is some reason to suspect that these predictions concerning capital were derived largely on an *a priori* basis from his theories of value, wages, and surplus value. The concentration of the growing capital of the system in the hands of a dwindling number of magnates was useful, as a concept, in another thesis-antithesis arrangement, with the increasing misery of the proletariat as the opposing factor.

### *The Increasing Misery of the Proletariat*

*Explanation of Increasing Misery* The downtrodden workers or members of the proletariat grow increasingly miserable in one sense because, with the wages of labor held down to a subsistence level, all increases in the efficiency and productivity of the capitalistic system and in its total income go to swell the amount of surplus value received by the exploiting bourgeoisie. To a great extent, however, Marx did not have this matter in mind in referring to the increasing misery of the proletariat. He meant instead the fact that, as the members of the proletariat increased because of the elimination of the smaller bourgeoisie, the relative need for labor in the industries and businesses of the system, as operated by the capitalist employers, tended to decline. The increased use of machinery tended to displace workers and reduce the direct labor requirements of the industries and businesses of the system. As individual enterprises increased in size, the proportion of constant capital to total capital also increased, and there was a relative decline in the amount of variable capital which was used to make wage payments.

to workers. Finally, the recurring crises of business depressions added greatly to the sum total of unemployment, and many of the cyclically unemployed were unable to regain employment after each depression came to an end. All these conditions tended to create a great reserve of labour or relative overpopulation, and in this situation the misery of the proletariat as a group could only increase.

As Marx explained the process:

The specifically capitalist mode of production, the development of the productive power of labour corresponding to it, and the change thence resulting in the organic composition of capital, do not merely keep pace with the advance of accumulation, or with the growth of social wealth. They develop at a much quicker rate, because mere accumulation, the absolute increase of the total social capital, is accompanied by the centralisation of the individual capitals of which that total is made up, and because the change in the technological composition of the additional capital goes hand in hand with a similar change in the technological composition of the original capital. With the advance of accumulation, therefore, the proportion of constant to variable capital changes. If it was originally say 1 : 1, it now becomes successively 2 : 1, 3 : 1, 4 : 1, 5 : 1, 7 : 1, etc., so that as the capital increases, instead of  $\frac{1}{2}$  of its total value, only  $\frac{1}{3}$ ,  $\frac{1}{4}$ ,  $\frac{1}{5}$ ,  $\frac{1}{6}$ ,  $\frac{1}{7}$ , etc., is transformed into labour-power and, on the other hand,  $\frac{2}{3}$ ,  $\frac{3}{4}$ ,  $\frac{4}{5}$ ,  $\frac{5}{6}$ ,  $\frac{6}{7}$ , into means of production. Since the demand for labour is determined not by the amount of capital as a whole, but by its variable constituent alone, that demand falls progressively with the increase of the total capital, instead of, as previously assumed, rising in proportion to it. It falls relatively to the magnitude of the total capital, and at an accelerated rate, as this magnitude increases. This accelerated relative diminution of the variable constituent, that goes along with the accelerated increase of the total capital, and moves more rapidly than this increase, takes the inverse form, at the other pole, of an apparently absolute increase of the labouring population, an increase always moving more rapidly than that of the variable capital or the means of employment. But in fact, it is capitalistic accumulation itself that constantly produces, and produces in direct ratio of its own energy and extent, a relatively redundant population of labourers, i.e., a population of greater extent than suffices for the average needs of the self-expansion of capital, and therefore a surplus-population.<sup>24</sup>

The labouring population therefore produces, along with the accumulation of capital produced by it, the means by which itself is made relatively superfluous, is turned into a relative surplus population, and it does this to an always increasing extent. This is a law of population peculiar to the capitalist mode of production, and in fact every special historic mode of production has its own special laws of population historically valid within its limits alone. An abstract law of population exists

<sup>24</sup> Karl Marx, *Capital*, Volume I, pp. 690-691.

for plants and animals only, and only in so far as man has not interfered with them But if a surplus labouring population is a necessary product of accumulation or of the development of wealth on a capitalist basis, this surplus population becomes, conversely, the lever of capitalististic accumulation, nay, a condition of existence of the capitalist mode of production It forms a disposable industrial reserve army, that belongs to capital quite as absolutely as if the latter had bred it at its own cost Independently of the limits of the actual increase of population, it creates, for the changing needs of the self expansion of capital, a mass of human material always ready for exploitation<sup>15</sup>

Increases in the size of the industrial reserve army are connected with cyclical fluctuations as well as with the growth and changing technical composition of capital

The course characteristic of modern industry, viz., a decennial cycle (interrupted by smaller oscillations), of periods of average activity, production at high pressure, crisis and stagnation, depends on the constant formation, the greater or less absorption, and the reformation of the industrial reserve army of surplus population In their turn, the varying phases of the industrial cycle recruit the surplus population, and become one of the most energetic agents of its reproduction<sup>16</sup>

Again

The industrial reserve army, during the periods of stagnation and average prosperity, weighs down the active labour-army, during the periods of overproduction and paroxysm, it holds its pretensions in check Relative surplus population is therefore the pivot upon which the law of demand and supply of labour works It confines the field of action of this law within the limits absolutely convenient to the activity of exploitation and to the domination of capital<sup>17</sup>

The existence of the industrial reserve army is also closely connected with the methods which the capitalist-employers use in extracting surplus value from the workers

The over-work of the employed part of the working class swells the ranks of the reserve, whilst conversely the greater pressure that the latter by its competition exerts on the former, forces these to submit to over-work and to subjugation under the dictates of capital The condemnation of one part of the working class to enforced idleness by the over work of the other part, and the converse, becomes a means of enriching the individual capitalists, and accelerates at the same time the production of the industrial reserve army on a scale corresponding with the advance of social accumulation<sup>18</sup>

<sup>15</sup> *Ibid.*, pp. 692 693

<sup>16</sup> *Ibid.*, p. 694

<sup>17</sup> *Ibid.*, p. 701

<sup>18</sup> *Ibid.*, p. 698

There was no doubt in Marx's mind as to the effects of all these things on the status and general welfare of the proletariat as a whole. As Marx said in a famous passage

Within the capitalist system all methods for raising the social productivity of labour are brought about at the cost of the individual labourer, all means for the development of production transform themselves into means of domination over and exploitation of, the producers, they mutilate the labourer into a fragment of a man, degrade him to the level of an appendage of a machine, destroy every remnant of charm in his work and turn it into a hated toil, they estrange from him the intellectual potentialities of the labour-process in the same proportion as science is incorporated in it as an independent power, they distort the conditions under which he works, subject him during the labour process to a despotism the more hateful for its meanness, they transform his life-time into working-time, and drag his wife and child beneath the wheels of the Juggernaut of capital. But all methods for the production of surplus value are at the same time methods of accumulation, and every extension of accumulation becomes again a means for the development of these methods. It follows therefore that in proportion as capital accumulates, the lot of the labourer, be his payment high or low must grow worse. The law, finally, that always equilibrates the relative surplus population, of industrial reserve army to the extent and energy of accumulation, this law rivets the labourer to capital more firmly than the wedges of Vulcan did Prometheus to the rock. It establishes an accumulation of misery, corresponding with the accumulation of capital. Accumulation of wealth at one pole is, therefore, at the same time accumulation of misery, agony of toil, slavery, ignorance, brutality, mental degradation, at the opposite pole.<sup>19</sup>

*The Actual Validity of the Prediction* We must now attempt to see whether the working classes or proletariat under capitalism have actually suffered the horrid fate of increasing misery which Marx prophesied for them. The answer depends in part upon the meaning which is attached to "increasing misery". Does it mean that the workers, considered entirely by themselves, grow worse off economically through time? Or does it mean that the workers, while holding their own in regard to real wages or standards of living, grow worse off in relation to the bourgeoisie because the gap between rich and poor widens instead of contracting? In other words, is it absolute increasing misery or relative increasing misery? There is quite general agreement that Marx usually meant absolute increasing misery, but, if this is true, there are some theoretical matters to be considered.

<sup>19</sup> *Ibid.*, pp. 708-709

In the first place, how do individuals, who are on a bare subsistence standard of living to begin with, become increasingly miserable? How can they? It would seem that individuals who are on a subsistence standard of living could only maintain or improve their economic lot. If their condition changed for the worse, they could no longer subsist and would presumably depart this life for a better one. But, it may be objected, Marx did not mean that employed workers would suffer increasing misery. He meant that there would be increasing misery for the proletariat as a whole, because, as the proletariat increased in size, an ever smaller proportion of its members would be needed for work in industry and business because of the changing organic or technical composition of capital and increased use of machinery. However, this does not help us very much. If only a part of the members of the proletariat are employed and those who are employed still receive subsistence wages, how do the unemployed members of the proletariat manage to live? If the employed members of the group shared their subsistence wages with the unemployed members, they themselves would be unable to live. We know, of course, the modern answer to this question in terms of unemployment insurance, direct relief, PWA, WPA, and other things, but Marx could hardly have foreseen these developments.

Again, there are some theoretical objections to the Marxian process by means of which the industrial reserve army of unemployed is to be created. In the first place, we have seen that it is a rather inadequate short-run opinion which holds that labor is displaced, on the whole, by machinery. Actually, over any considerable period of time, the introduction of labor-saving machinery creates, or permits the creation of, as much employment as it destroys. Again, there is nothing about a decline in the relative proportion of variable capital to constant capital which necessarily produces a decline in the total demand for labor and increased unemployment even if we agree with Marx that variable capital is the only source of the demand for labor. In other words, the volume of employment would still depend upon the absolute amount of variable capital and not upon the proportion of variable capital to constant capital or to total capital. For example, if a firm formerly had a total capital of \$100,000 composed in equal parts of constant and variable capital, and now has a total capital of \$300,000 composed of one-fourth variable capital and three-fourths constant capital, variable

capital has decreased by one-half as a *proportion* of total capital but it has increased in *absolute amount* from \$50,000 to \$75,000. If the workers receive subsistence wages in both cases, it is obvious that \$75,000 a year will employ more workers than \$50,000 a year regardless of the proportions of these sums to total capital. There is nothing about a decline in the proportion of variable capital which needs to reduce the total demand for labor and increase unemployment. These results would occur only if the shift to constant capital went forward at a more rapid rate than total capital accumulation, and on this point we have no evidence other than Marx's assertions.

If increasing misery is interpreted in the absolute sense, i.e., with exclusive reference to the economic lot of the workers themselves, there is little evidence in our capitalistic system today that Marx's prediction has come true. To be sure, we have various groups of workers even in modern times who are at or near a subsistence standard of living, and it may even be true that there are some small groups today which are worse off than their ancestors were in Marx's time, but on the whole there is general agreement that the average real wages and standard of living of the workers of this country have improved immensely from Marx's day to the present time. One study of the purchasing power of hourly wages in all industries in the United States from 1850 to 1912 indicated that real hourly wages had increased from an index number of 46.8 to one of 103, or by about 120 per cent.<sup>20</sup> Another study of real wages in the United States concluded that there had been an increase of more than 300 per cent in the real wages of the American worker from 1791 to 1932.<sup>21</sup> Somewhat less striking but on the whole comparable increases in real wages have occurred in other capitalistic countries. In addition to such increases in real wages, our workers have received an increasing volume of direct social services from various governmental units. On the other hand, these gains may have been cancelled to some extent by such factors as increasing economic insecurity. We always seem to have an unemployment problem in modern times, and in times of severe depression it is a monstrous problem. There is definitely something wrong with an economic system that cannot avoid a large total of unemployment,

<sup>20</sup> W. I. King, *The Wealth and Income of the People of the United States*, New York: The Macmillan Company, 1915, pp. 189-190.

<sup>21</sup> R. S. Tucker, "Real Wages Under Laissez Faire," in *Barron's*, October 23, 1933.

but our judgment of unemployment as a source of increasing misery should be tempered to some extent by the knowledge that people who are "on WPA" in modern times have higher standards of living than the full-fledged worker of Marx's day.

If increasing misery is interpreted in the relative sense, a somewhat stronger argument can be made for the validity of Marx's prediction. While some interpreters of Marx insist that he could not have been referring to relative increasing misery, it seems obvious to us that he did employ this concept at times, as, for example, when he spoke of all increases in the productivity, efficiency, and total income of the capitalistic system going to swell the amount of surplus value received by the bourgeoisie while the workers lagged behind on their subsistence wages. On the basis of this concept, it is possible to argue that the workers of our country have become increasingly miserable in the sense that the gap between their average incomes and those of the real magnates of capitalism has widened instead of narrowing since Marx's time. Of course, we do not have reliable data on the distribution of the national income among persons as of 1850, but studies that have been made from 1918 to the present day certainly do not indicate that inequality in the personal distribution of the national income (before taxes are paid) is growing any less as time goes on. However, while the prediction of relative increasing misery may be more nearly valid than that of absolute increasing misery, it is not as powerful an indictment of the capitalistic system, and the existence of increasing misery in the relative sense may be less likely to lead to the breakdown of capitalism.

The supporters of Marx have in general been rather disturbed about his prediction of increasing misery for the proletariat. Some have almost denied that he ever made the prediction while others have indicated that, even if he made the prediction, he did not really mean it. It is sometimes contended that increasing misery should be interpreted in a psychological rather than a material sense. That is, the workers today are better off than they used to be but they feel worse off or think that they are worse off. They are more conscious than formerly of their relatively lowly position and of their lack of control over their own lives. The ratio of their satisfied wants to their total wants is lower than it was many years ago, not because they are less well supplied with goods than formerly but because they are conscious of a greater range of wants.

Concern is also sometimes expressed over the prediction of increasing misery for the proletariat because it is thought that this prediction is inconsistent with Marx's other prediction that the proletariat will one day rise up and take over the capitalistic system. How, it is asked, can the proletariat become more miserable and also stronger at the same time? How can it become an increasingly strong revolutionary force though weaker in other respects? Cole, for example, mentions this problem and goes on to reject the relative concept of increasing misery as inconsistent with Marx and the absolute concept of increasing misery as inconsistent with the facts. His own solution is that Marx would have admitted that the wages and standards of living of the proletariat may improve so long as the capitalistic system is advancing and developing, but that Marx meant that the economic lot of the proletariat would become worse after the capitalistic system had reached the peak of its development and had begun to go downhill—a development which is already in process.<sup>22</sup>

*The Prospective Validity of the Prediction.* On the whole, the prediction of the increasing misery of the proletariat has turned out to be one of the least satisfactory of the Marxian predictions but there may have been good reasons why Marx should have made the prediction at the time when he was forming his opinions. In his studies of the first few decades of economic life after the Industrial Revolution in England, it is difficult to see how Marx could have concluded that modern capitalism had been or would be a boon to the workers. Large numbers of workers had been gathered from the country and crowded into the industrial towns and cities which had, at best, most precarious facilities for receiving and caring for them. The workers sometimes lived 15 or 20 to the small poorly constructed room under incredibly bad sanitary conditions. They worked enormous working-days in jerry-built factories, with almost unbelievable risks to life, limb, and general health. And then reward for all this consisted of extremely low wages and an untimely end. But nothing that we can say on this subject is likely to be more effective than Marx's own illustrations. Let us consider some of the evidence on which he based his conclusion and prediction.

Quoting a report on the lace trade, Marx said

there was an amount of privation and suffering among that portion of the population connected with the lace trade, unknown in other parts

<sup>22</sup> G. D. H. Cole, *What Marx Really Meant*, p. 110

of the kingdom, indeed, in the civilized world Children of nine or ten years are dragged from their squalid beds at two, three, or four o'clock in the morning and compelled to work for a bare subsistence until ten eleven, or twelve at night their limbs wearing away, their frames dwindling their faces whitening, and then humanity absolutely sinking into a stonelike torpor, utterly horrible to contemplate.<sup>23</sup>

Again, in speaking of the pottery trade, Marx said

From the children we may form an opinion as to the adults, especially the girls and women, and thus in a branch of industry by the side of which cotton spinning appears an agreeable and healthful occupation William Wood 9 years old, was 7 years and 10 months old when he began to work He 'ran moulds' (carried ready moulded articles into the drying room, afterwards bringing back the empty mould) from the beginning He came to work every day in the week at 6 A.M., and left off about 9 P.M. 'I work till 9 o'clock at night six days in the week. I have done so seven or eight weeks' Fifteen hours of labour for a child of 7 years old! J Murray 12 years of age, says "I turn jiggers, and run moulds I come at 6. Sometimes I come at 4. I worked all last night, till 6 o'clock this morning I have not been in bed since the night before last There were eight or nine other boys working last night All but one have come this morning I get 3 shillings and six pence I do not get any more for working at night I worked two nights last week" Fernyhough, a boy of ten "I have not always an hour (for dinner) I have only half an hour sometimes, on Thursday, Friday, and Saturday"<sup>24</sup>

From a doctor's report, Marx notes

The potters as a class, both men and women, represent a degenerated population both physically and morally They are, as a rule, stunted in growth, ill shaped, and frequently ill formed in the chest, they become prematurely old, and are certainly short lived, they are phlegmatic and bloodless, and exhibit their debility of constitution by obstinate attacks of dyspepsia, and disorders of the liver and kidneys, and by rheumatism But of all diseases they are especially prone to chest disease to pneumonia, phthisis, bronchitis, and asthma One form would appear peculiar to them, and is known as potter's asthma, or potter's consumption Scrofulula attacking the glands, or bones, or other parts of the body is a disease of two thirds or more of the potters That the 'degenerescence' of the population of this district is not even greater than it is, is due to the constant recruiting from the adjacent country, and intermarriage with more healthy races<sup>25</sup>

Of the baking trade, it is said

<sup>23</sup> Karl Marx, *Capital*, Volume I, p 268

<sup>24</sup> *Ibid.*, pp 269 270

<sup>25</sup> *Ibid.*, pp 270 271

During what is called "the London season," the operatives belonging to the "full-priced" bakers at the West End of the town, generally begin work at 11 p.m., and are engaged in making the bread, with one or two short (sometimes very short) intervals of rest, up to 8 o'clock the next morning. They are then engaged all day long, up to 4, 5, 6, and as late as 7 o'clock in the evening carrying out bread, or sometimes in the afternoon in the bakehouse again, assisting in the biscuit baking. They may have, after they have done their work, sometimes five or six, sometimes only four or five hours' sleep before they begin again. On Fridays they always begin sooner, some about ten o'clock, and continue in some cases, at work, either in making or delivering the bread up to 8 p.m. on Saturday night, but more generally up to 4 or 5 o'clock, Sunday morning. The men employed by the underselling masters (who sell their bread under the "full price," and who, as already pointed out, comprise three-fourths of the London bakers) have not only to work on the average longer hours, but their work is almost entirely confined to the bakehouse. Towards the end of the week the men begin on Thursday night at 10 o'clock, and continue on with only slight intermission until late on Saturday evening.<sup>26</sup>

And finally, one of Marx's more famous illustrations

In the last week of June, 1863, all the London daily papers published a paragraph with the "sensational" heading "Death from simple over-work." It dealt with the death of the milliner, Mary Anne Walkley, 20 years of age, employed in a highly-respectable dressmaking establishment, exploited by a lady with the pleasant name of Elise. The old, often told story, was once more recounted. This girl worked, on an average, 16½ hours, during the season often 30 hours, without a break, whilst her failing labour-power was revived by occasional supplies of sherry, port, or coffee. It was just now the height of the season. It was necessary to conjure up in the twinkling of an eye the gorgeous dresses for the noble ladies bidden to the ball in honour of the newly-imported Princess of Wales. Mary Anne Walkley had worked without intermission for 26½ hours, with 60 other girls, 30 in one room, that only afforded  $\frac{1}{3}$  of the cubic feet of air required for them. At night, they slept in pens in one of the stifling holes into which the bedroom was divided by partitions of board. And this was one of the best millinery establishments in London. Mary Anne Walkley fell ill on the Friday, died on Sunday, without, to the astonishment of Madame Elise, having previously completed the work in hand. The doctor, Mr Keys, called too late to the death-bed, duly bore witness before the coroner's jury that "Mary Anne Walkley had died from long hours of work in an over crowded workroom, and a too small and badly-ventilated bedroom." In order to give the doctor a lesson in good manners, the coroner's jury thereupon brought in a verdict that "the deceased had died of apoplexy, but there was reason to fear that her death had been accelerated by over work in an over crowded workroom,

<sup>26</sup> *Ibid.*, p. 276

etc "Our white slaves" cried the "Morning Star" the organ of the free-traders, Cobden and Bright "our white slaves who are toiled into the grave, for the most part silently pine and die"

"It is not in dressmaker's rooms that working to death is the order of the day, but in a thousand other places, in every place I had almost said, where a 'thriving business' has to be done We will take the blacksmith as a type If the poets were true, there is no man so hearty, so merry, as the blacksmith, he rises early and strikes his sparks before the sun, he eats and drinks and sleeps as no other man Working in moderation, he is, in fact, in one of the best of human positions, physically speaking But we follow him into the city or town, and we see the stress of work on that strong man, and what then is his position in the death rate of his country In Marylebone blacksmiths die at the rate of 31 per thousand per annum, or 11 above the mean of the male adults of the country in its entirety The occupation instinctive almost as a portion of human art, unobjectionable as a branch of human industry, is made by mere excess of work, the destroyer of man He can strike so many blows per day, walk so many steps, breathe so many breaths produce so much work and live an average, say of fifty years he is made to strike so many more blows, to walk so many more steps, to breathe so many more breaths per day, and to increase altogether a fourth of his life He meets the effort, the result is, that producing for a limited time a fourth more work he dies at 37 for 30 "<sup>27</sup>

These and many other illustrations presented in *Capital* indicate the sorry plight of the workers in various unregulated trades in Marx's day The cases have not been invented by Marx, for, as a general rule, he quotes from Parliamentary reports, and reports of investigating commissions If conditions such as those described still prevailed in England in 1850 or 1860, surely Marx had some reason for deciding that modern capitalism had resulted and probably would continue to result in the increasing misery of the proletariat, even though his prediction has not come true, in any absolute sense, in practice

### *The Last Days of Capitalism*

**Finance Capital** Marx had no doubt that these contradictions of economic life under capitalism—between the increasing wealth of the bourgeoisie and the increasing misery of the proletariat, and between the growing productive power of the system and the limited consuming power of the toiling masses based on subsistence incomes—would eventually cause the breakdown of the capitalistic

<sup>27</sup> *Ibid.*, pp 280 282

system Marx himself, however, was not especially definite with respect to the details of the last days of capitalism, and many of these details had to be filled in by various supporters and interpreters of Marx. As the workers fall into increasing misery and as more and more severe crises or business depressions occur, capital becomes centralized in fewer and fewer hands until eventually monopolistic conditions prevail in each field of industry and business. This result is followed by an alliance or merging of bank capital with industrial capital and the establishment of a financial oligarchy. In this stage of capitalism, the capitalist becomes a pure parasite. The control of production rests in the hands of financial magnates and it is exercised, through monopolistic industrial concerns, to create not merely surplus value, but monopolistic surplus value.

*Capitalistic Imperialism* But, for all this, the capitalistic system operates less and less satisfactorily because of the increasing severity of its internal conflicts and contradictions. However, the system is saved for the time being by a further development. The financial magnates, with their control over industrial production, reach out beyond the boundaries of the individual capitalistic system and the result is capitalistic imperialism. Each capitalistic country tries to bring other backward areas under its control and to use these areas as markets for products which cannot be sold profitably at home, as sources of necessary materials, as parking spaces for surplus population, and as places in which capital can still be invested profitably. This capitalistic imperialism might prolong the life of the capitalistic system in any one country indefinitely, but in actual practice the leading capitalistic countries all try the same procedure and, in spite of international alliances and monopolies, international antagonisms result which lead to severe imperialistic wars between the nations. Eventually, each mature capitalistic system breaks down, either in a great war or a severe depression, a revolution follows, and the proletariat seizes control of state, government, and economic system.

Except for the eventual breakdown and revolution, this description seems to be fairly well fitted to what has been going on in the modern world. Alliances between industrial capital and bank capital are said to exist in the United States. The National Resources Committee recently found that companies controlling 62 per cent of the total assets of the 200 largest nonfinancial and 50 largest finan-

cial companies were members of large "interest groups," which combined industrials, railroads, and public utilities with commercial and investment banking houses in informal communities of interest. The assets controlled by these interest groups varied from \$2,000,-000,000 for the smallest to \$30,000,000,000 for the largest.<sup>28</sup> There was also said to be much overlapping and interconnection between these interest groups. There can be no doubt about the imperialistic policies which have been followed by the leading capitalistic nations or about the severe wars which have occurred between these nations in modern times. These wars perhaps cannot be traced entirely to the struggle for international investments, markets, and materials, but this struggle has undoubtedly played a part in bringing on these "world wars."

*The End of Capitalism.* At any rate, Marx was sure of the eventual breakdown of the capitalistic system and of the revolution which would transform it into a better society. As he said, in a brief review of the events leading to the downfall of capitalism:

As soon as this process of transformation has sufficiently decomposed the old society from top to bottom, as soon as the labourers are turned into proletarians, their means of labour into capital, as soon as the capitalist mode of production stands on its own feet, then the further socialisation of labour and further transformation of the land and other means of production into socially exploited and, therefore, common means of production, as well as the further expropriation of private proprietors takes a new form. That which is now exploited is no longer the labourer working for himself, but the capitalist exploiting many labourers. This expropriation is accomplished by the action of the immanent laws of capitalistic production itself by the centralisation of capital. One capitalist always kills many. Hand in hand with this centralisation, or this expropriation of many capitalists by few, develop, on an ever extending scale, the cooperative form of the labour-process, the conscious technical application of science, the methodical cultivation of the soil, the transformation of the instruments of labour into instruments of labour only usable in common, the economising of all means of production by their use as the means of production of combined, socialised labour, the entanglement of all peoples in the net of the world market, and this the international character of the capitalistic regime. Along with the constantly diminishing number of the magnates of capital, who usurp and monopolise all advantages of this process of transformation, grows the mass of misery, oppression, slavery, degradation, exploitation; but with this too grows the revolt of the working class, a class always increasing in numbers, and disciplined, united, organised by the very mechanism of the

<sup>28</sup> National Resources Committee, *The Structure of the American Economy*, pp. 306-317.

process of capitalist production itself. The monopoly of capital becomes a fetter upon the mode of production, which has sprung up and flourished along with, and under it. Centralisation of the means of production and socialisation of labour at last reach a point where they become incompatible with their capitalist integument. This integument is burst asunder. The knell of capitalist private property sounds. The expropriators are expropriated.<sup>20</sup>

### QUESTIONS

1. "Capitalistic production begets, with the inevitability of a law of nature, its own negation. The fate of capitalism is inevitable, since it is sealed by the very processes which the system itself inherently generates." Explain.
2. "While the Marxian predictions concerning the consequences of capitalistic production are often separated for purposes of emphasis, they are really inseparable. One cannot discuss, for example, the concentration and centralization of capital without bringing in such other matters as the increasing severity of business cycles and the increasing misery of the proletariat." Explain fully.
3. Select one of the Marxian predictions as to the consequences of capitalistic production and explain (a) how Marx expected this particular result to be accomplished, (b) whether the prediction seems to have come true in the economic system of the United States, and (c) whether there were any reasons, as of the time when Marx reached his conclusions, for expecting the prediction to be valid.
4. On the basis of economic conditions of the present day in the United States defend or attack Marx's predictions as to the consequences of capitalistic production.
5. "Several of Marx's predictions with regard to the consequences of capitalistic production may have seemed much more plausible as of about the year 1850 than they do today." Do you agree? Explain.
6. Explain the Marxian theories with respect to the causes of business cycles under capitalism.
7. Why were business cycles supposed to become increasingly severe, according to Marx? Have they actually done so in the United States? Explain.
8. Distinguish between the concentration and centralization of capital.
9. "The process by means of which the centralization of capital takes place is closely connected with the recurrence of business depressions." Explain.
10. "If Marx were alive today, he would be satisfied with the concentration and centralization of capital in the United States as a fulfillment of his prediction." Discuss.

<sup>20</sup> Karl Marx, *Capital*, Volume I, pp. 836-837.

- 11 Explain the various phases of the process by means of which, according to Marx, the proletariat becomes increasingly miserable under capitalism
- 12 "There are both theoretical and practical objections to Marx's prediction of the increasing misery of the proletariat" Explain
- 13 "There is little evidence in our capitalistic system today that Marx's prediction with respect to the increasing misery of the proletariat has come true" Do you agree? Explain
- 14 "At the time when Marx was forming his opinions, there were many good reasons why he should have predicted the increasing misery of the proletariat" Explain
- 15 "Marx was inconsistent in arguing that, while workers were being forced into increasing misery, the rate of profits tended to decline" Show whether you agree
- 16 "The Marxian prediction as to the increasing misery of the proletariat has not come true on an absolute basis, though it may be argued that the prediction has actually worked out on a relative basis Just the opposite is true of the prediction as to the increasing severity of business cycles" Show whether you agree
- 17 Summarize Marx's discussion of the last days of capitalism

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## CHAPTER 30

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### **THE REVOLUTION AND AFTER**

THE breakdown of capitalism is inevitable, but that breakdown does not by itself produce the ideal society of the future. Unless there were strong hands ready to seize the reins of control, the breakdown might lead only to chaos. Fortunately, the bourgeoisie in leading the capitalistic system to its eventual doom have produced a strong opposition class which is ready to take over. As the *Communist Manifesto* said

The essential condition for the existence, and for the sway of the bourgeois class, is the formation and augmentation of capital, the condition for capital is wage-labor. Wage labor rests exclusively on competition between the laborers. The advance of industry, whose involuntary promoter is the bourgeoisie, replaces the isolation of the laborers, due to competition, by their revolutionary combination due to association. The development of Modern Industry therefore, cuts from under its feet the very foundation on which the bourgeoisie produces and appropriates products. What the bourgeoisie therefore produces, above all, are its own grave diggers. Its fall and the victory of the proletariat are equally inevitable.<sup>1</sup>

#### *The Revolution*

**The Necessity for Revolution** If the proletariat is to take control after the breakdown of capitalism, will it be able to do so by peaceful means or will a revolution be necessary? On this point, as on many others, Marx had more than one opinion, but his majority opinion clearly was that revolution was necessary. No matter how serious the final collapse into which the bourgeoisie have managed to lead the capitalistic system they will be unwilling to relinquish control because they could not imagine any other system in which they would be as well treated. They had acquired originally then

<sup>1</sup> Marx Engels, *The Communist Manifesto*, p. 29

capital by forceful measures and expropriation, and they would lose it only by similar methods Having lived by the sword, they would have to die by the sword Moreover, the bourgeoisie have control over the government and its armed forces and will use them to protect their position The need for revolution is also indicated by the thoroughness of the changes which the capitalistic system requires As Marx once said "With us it is not a matter of reforming private property, but of abolishing it, not of hushing up the class antagonism, but of abolishing the classes, not of ameliorating the existing society, but of establishing a new one"<sup>2</sup> Changes of this scope and magnitude could hardly be accomplished by peaceful, evolutionary means

There is considerable evidence not only that Marx considered a revolution to be necessary, but also that revolution to him meant a violent and bloody overthrow of the existing regime and not merely sudden change Toward the end of the *Communist Manifesto*, the authors said "The Communists disdain to conceal their views and aims They openly declare that their ends can be attained only by the forcible overthrow of all existing social conditions Let the ruling classes tremble at a Communist revolution"<sup>3</sup> In his newspaper the *Neue Rheinische Zeitung*, Marx said "When our turn comes, revolutionary Terrorism will not be sugar-coated There is but one way of simplifying, shortening, concentrating the death agony of the old society as well as the bloody labor of the new world's birth—revolutionary Terrorism"<sup>4</sup> In an address to the Communist League in 1850, Marx said "Far from opposing so called excesses, and making examples of hated individuals or public buildings to which hateful memories are attached by sacrificing them to popular revenge, such deeds must not only be tolerated but their execution must be taken in hand"<sup>5</sup> Still later, Marx said "To take vengeance for the misdeeds of the ruling class, there existed in the Middle Ages in Germany a secret tribunal called the *Vehmgericht* If a red cross was seen marked on a house, people knew that its owner was doomed by the *Vehm* All the houses in Europe are now

<sup>2</sup> Karl Marx, "Address to the Communist League," *Handbook of Marxism* E Burns compiler New York Random House, 1935, p 64 Reprinted by permission of the publishers

<sup>3</sup> Marx Engels, *The Communist Manifesto*, p 58

<sup>4</sup> Quoted in J E LeRossignol *From Marx to Stalin*, p 321

<sup>5</sup> *Handbook of Marxism*, p 66 Reprinted by permission of Random House, New York

marked by the mysterious red cross History is the judge, its executioner, the proletariat".<sup>6</sup> Finally, toward the end of the first volume of *Capital*, Marx said "Force is the midwife of every old society pregnant with a new one".<sup>7</sup>

**The Locus of the Revolution** Where would the revolution strike first? Marx, true to his general analysis, held that it would come first in one of the most highly developed capitalistic countries. He seemed to vary between Germany and England as his first choice. In 1844, both Marx and Engels seemed fairly sure that the revolution would come in England as a result of the Chartist movement. However, in the *Communist Manifesto*, Marx and Engels said

The Communists turn their attention chiefly to Germany, because that country is on the eve of a bourgeois revolution, that is bound to be carried out under more advanced conditions of European civilization and with a much more developed proletariat, than that of England was in the seventeenth, and of France in the eighteenth century, and because the bourgeois revolution in Germany will be but the prelude to an immediately following proletarian revolution.<sup>8</sup>

Much later still, Marx again selected England as the most likely spot for revolution. He said

Although the revolutionary initiative will probably come from France, England alone can serve as the lever of a serious economic revolution. It is the only country where there are no more peasants and where property in land is concentrated in a few hands. It is the only country where the capitalist form—that is to say combined labour on a large scale under capitalist employers—has invaded practically the whole of production. It is the only country where the great majority of the population consists of wage labourers. It is the only country where the class struggle and the organization of the working class through the trade unions has acquired a certain degree of maturity and universality. As a result of its dominating position in the world market, it is the only country where every revolution in its economic conditions must react directly on the entire world. If this country is the classic seat of landlordism and capitalism, by virtue of that fact it is also here that the material conditions of their destruction are most highly developed. England cannot be treated simply as one country among a number of other countries. She must be treated as the metropolis of capitalism.<sup>9</sup>

<sup>6</sup> Marx-Engels, *Selected Correspondence*, p. 91. Reprinted by permission of International Publishers, New York.

<sup>7</sup> Karl Marx, *Capital*, Volume I, p. 821.

<sup>8</sup> Marx-Engels, *The Communist Manifesto*, p. 58.

<sup>9</sup> Karl Marx, *Letters to Dr. Kugelmann* New York International Publishers, 1934, pp. 106-107.

While Marx persisted in thinking that the revolution would come first in some highly developed capitalistic system, some of his modern disciples have disagreed with this opinion. Lenin, for example, had no doubt that the revolution might occur in a country with quite ordinary capitalistic development or even in a backward country such as Russia in which the capitalist mode of production was but little developed and most of the people were peasants. From this point of view, the capitalistic countries resembled a chain which might well be expected to give way at its weakest link and not a crate of apples in which the ripest and most mature fruits might be expected to decay first.

*The Time of the Revolution.* As to the time when the revolution would come, Marx could only say that it would come when the time was ripe for it. His general attitude was expressed in the following words:

No social order ever disappears before all the productive forces, for which there is room in it, have been developed, and new higher relations of production never appear before the material conditions of their existence have matured in the womb of the old society. Therefore, mankind always takes up only such problems as it can solve, since, looking at the matter more closely, we will always find that the problem itself arises only when the material conditions necessary for its solution already exist or are at least in the process of formation.<sup>10</sup>

In the first half of his life, Marx on several occasions thought that the time was getting ripe for revolution in this country or that, but his hopes and expectations were always blighted in practice.

After several such experiences, he realized that the process by means of which the capitalistic system moves toward breakdown and revolution is an extremely slow one and that nothing is gained by trying to hurry it or by attempting revolution before the time is ripe. By 1863, he could write to Engels:

Only the little German *Spiessgesellen* (petty bourgeois), who measure world history by the yard and the latest "interesting news in the paper" could imagine that in developments of such magnitude twenty years are more than a day—though later on days may come again in which twenty years are embodied.<sup>11</sup>

<sup>10</sup> Karl Marx, *A Contribution to the Critique of Political Economy*, pp. 12-13.

<sup>11</sup> Marx-Engels, *Selected Correspondence*, p. 147. Reprinted by permission of International Publishers, New York.

Late in his life, Marx apparently lost faith to some extent in the coming of the revolution and even in the necessity for revolution. Thus, in 1872, he remarked

But we do not assert that the way to reach this goal is the same everywhere. We know that the institutions, the manners, and the customs of the various countries must be considered, and we do not deny that there are countries like England and America, and, if I understood your arrangements better, I might even add Holland, where the worker may attain his object by peaceful means. But not in all countries is this the case.<sup>12</sup>

Marx apparently had begun to realize that he had underestimated the significance of labor organizations, social legislation, and the political power of the workers. Several years after Marx's death, Engels freely admitted that he and Marx had been wrong in expecting the full-fledged proletarian revolution to occur in the middle of the nineteenth century. As he said

History has proved us, and all who thought like us, wrong. It has made it clear that the state of economic development on the Continent at that time was not, by a long way, ripe for the removal of capitalistic production.<sup>13</sup>

**Necessary Conditions for Revolution** If the proletariat is to rise up at the psychological moment and take over the state, government, and economic system of capitalism, there must be some way for the leaders of this great class to know when the time is ripe for revolution. How can it be determined when the great day is at hand? According to one interpreter of Marx, three conditions must be present in the economy if the revolution is to be considered imminent. First, there must be a breakdown of the forces of production and distribution in the capitalistic system. Second, there must be a "lack of immediate political homogeneity on the part of the ruling classes"—a condition which could readily exist in the midst of a severe crisis. Finally, there must be "spontaneous manifestations of class consciousness and struggle, such as strikes, riots, and mass demonstrations."<sup>14</sup>

<sup>12</sup> Quoted in H. W. Laidler, *A History of Socialist Thought*. New York: The Thomas Y. Crowell Company, 1927, p. 194.

<sup>13</sup> *Handbook of Marxism*, p. 79. Reprinted by permission of Random House, New York.

<sup>14</sup> Sidney Hook, *Towards the Understanding of Karl Marx*. New York: The John Day Company, 1933, p. 276.

After considering these essential conditions for revolution, one might be moved to wonder why there was not a revolution in the United States in the depression years following 1929. Although our capitalistic system of production and distribution did not break down completely in this depression, the breakdown was probably more nearly complete than it ever had been before. Certainly there was widespread disagreement among the leaders of our economy as to what should be done in the crisis in order to attain recovery and prosperity. Some men said that recovery could never come until wages and other costs had been cut enough to make profitable production possible once more. Other equally important spokesmen revealed that wages and consumer buying power in general should be maintained at a high level if recovery were to occur. Some said that the depression would be bottomless if left to its own devices and that additional strong governmental intervention and control would be necessary to induce recovery. Others said that the government was already playing too great a part in the economic life of the country and that recovery must wait upon the freeing of private business from the shackles of governmental control. Some blamed the depression on international influences and thought a higher protective tariff would lead the way to prosperity. Others contended that our policy of protectionism had played a considerable part in producing the depression and called for a free interchange of goods between this country and other countries.

No riots and mass demonstrations at all lacked. We all remember the embittered hosts who marched on Washington and were dispersed by the armed forces, and the farmers who removed their trusty rifles or shotguns from the wall and joined in armed bands to prevent sheriff's sales of farm property or to overturn milk and vegetable trucks to keep farm produce from reaching the depressed markets. And yet, in spite of all these things, no revolution occurred. What was lacking? Apparently, it was the absence of a large, downtrodden, well-organized, class conscious proletariat which was fatal to the hopes of revolution which anyone may have had. In the crisis, practically all Americans, from lowly worker or "reliever" to captain of industry, thought and acted as members of the middle class. As long as this is true, a capitalistic system can apparently survive almost any kinds of economic conditions.

### *The Dictatorship of the Proletariat*

***The Dictatorship as a Period of Transition*** Regardless of all arguments over the revolution, we shall now concede Marx his revolution (in theory) in order to catch a glimpse of the more satisfactory states of society which are to follow it. According to the Marxian theory the truly ideal state of society cannot emerge fully developed from the revolution. The classless commonwealth of anarchistic communism can be reached only after society has passed through a more or less extensive period of transition known as the dictatorship of the proletariat. As Marx said:

Between the capitalist and the communist systems of society lies the period of the revolutionary transformation of the one into the other. This corresponds to a political transition period, whose State can be nothing but the *revolutionary dictatorship of the proletariat*.<sup>15</sup>

Again

And now as to myself, no credit is due to me for discovering the existence of classes in modern society nor yet the struggle between them. Long before me bourgeois historians had described the historical development of this class struggle and bourgeois economists the economic anatomy of the classes. What I did that was new was to prove (1) That the *existence of classes* is only bound up with *particular, historic phases in the development of production*, (2) that the class struggle necessarily leads to the *dictatorship of the proletariat*, (3) that this dictatorship itself only constitutes the transition to the *abolition of all classes* and to a *classless society*.<sup>16</sup>

***Political Conditions*** A dictatorial government would be nothing new because, in the Marxian analysis, governments, regardless of their apparent organization, are always dictatorships in fact. The state, as always, would be under the control of the most powerful class of the times and would be used, as always, as an agency of oppression. After the revolution, however, the dominant class would be the proletariat, and it would use the power of the state to oppress the formerly powerful bourgeoisie. Obviously, the government which would exist under the dictatorship of the proletariat would be far from ideal, but some Marxian supporters, such as Lenin,

<sup>15</sup> Karl Marx, *The Gotha Program* New York: New York Labor News Company, 1925, p. 48. Reprinted by permission of the publishers.

<sup>16</sup> Marx-Engels, *Selected Correspondence*, p. 57 (Marx to Weydemeyer). Reprinted by permission of International Publishers, New York.

have contended that this government would at least be more democratic than that which had formerly existed under capitalism. Formerly, the few (bourgeoisie) oppressed the many (proletariat), but now the situation is reversed and the many oppress the few—and this, so it is said, is obviously fairer and more democratic. The bourgeoisie must be oppressed and suppressed.

In order to free humanity from wage slavery their resistance must be broken by force. It is clear that where there is suppression there is also violence; there is no liberty, no democracy. Democracy for the vast majority of the people, and suppression by force i.e., exclusion from democracy of the exploiters and oppressors of the people, this is the modification of democracy during the transition from capitalism to communism.<sup>17</sup>

It is the task of the dictatorship to destroy and eradicate completely all vestiges of the old capitalistic system, including, of course, capitalistic ideology. As Lenin said:

The dictatorship of the proletariat is the fiercest, sharpest, and most merciless of all of the new class against its more powerful enemy, the bourgeoisie, whose resistance is increased tenfold by its overthrow. The dictatorship of the proletariat is a stubborn struggle—sanguinary and bloodless, violent and peaceful, military and economic, educational and administrative—against the forces and traditions of the old society. The dictatorship of the proletariat is the domination of the proletariat over the bourgeoisie, a domination that is untrammeled by law and based on violence and enjoys the sympathy and support of the toiling and exploited masses.<sup>18</sup>

The justification of the violent transition period is found in the fact that it paves the way for the ideal classless society of the future.

Democracy is not identical with majority rule. No, democracy is a State which recognises the subjection of the minority to the majority, that is, in organization for the systematic use of violence by one class against the other, by one part of the population against another. But striving for Socialism, we are convinced that it will develop further into Communism, and, side by side with this, there will vanish all need for force, for the subjection of one man to another, of one section of society to another, since people will grow accustomed to observing the elementary conditions of social existence without force and without subjection.<sup>19</sup>

<sup>17</sup> V. I. Lenin, "The State and Revolution," *Handbook of Marxism*, p. 745. Reprinted by permission of Random House, New York.

<sup>18</sup> Quoted in J. Stalin, *Foundations of Leninism*. New York: International Publishers, 1932, pp. 47-50. Reprinted by permission of the publishers.

<sup>19</sup> V. I. Lenin, *Imperialism: The State and Revolution*. New York: The Vanguard Press, 1929, p. 187. Reprinted by permission of the publishers.

**Economic Features** The transformation of the bourgeois state into the proletarian state is accompanied by the transformation of the bourgeois economy into the proletarian economy, or of the system of capitalism into one of socialism. As in the case of the state or government, this transformation of the economic system means primarily a change in management rather than in fundamental methods and processes. The economic system will have the same agents of production as before, organized as before, and using familiar methods and practices of production. The most important change that has occurred is found in the fact that what was formerly the private property of the capitalist-employers is now the property of the proletarian state and, through the state, of the workers. The means of production are now socially owned, or at least are owned by the majority of society, the proletariat.

With the capitalists, landowners, and entrepreneurs gone, the proletarian state operates the economic system in the name of the workers. Workers in all sorts of ordinary jobs are not disturbed or displaced. Engineers, agonomists, research workers, and other technically trained workers continue in their positions and, obeying the armed workers instead of the capitalist-employers, work even better than before. With true Marxian disdain for the functions of management, it is said that the work of managers, foremen, bookkeepers, and other clerks, then "simple operations of watching, recording, and issuing receipts will be within reach of anybody who can read and write, and knows the first four arithmetical rules."<sup>20</sup> Needless to say, some individuals will be in more vital and responsible economic positions than others, but they will be kept from becoming "bureaucrats" because, in the beginning, they will be elected to office and will be subject to recall, and later on the workers will be rotated in office at rather frequent intervals.

While the economic system, during the dictatorship of the proletariat, will presumably have to operate as a planned economy, the writings of some Marxian followers seem to suggest that the economic system will operate almost automatically once the change of management from the bourgeoisie to the proletariat has been effected. Thus Lenin has said:

We have but to overthrow the capitalists to crush with the iron hand of the armed workers the resistance of these exploiters, to break the bureaucratic machine of the modern State—and we have before us a

<sup>20</sup> *Ibid.*, p. 205. Reprinted by permission of the Vanguard Press, New York.

highly technically fashioned machine freed of its parasites, which can quite well be set going by the united workers themselves, hiring their own technical advisers, and paying them all, as, indeed every "State" official with the usual workers' wage. Here is a concrete task, immediately practicable and realizable as regards all trusts, which would rid the workers of exploitation and which would make practical use of the experience which the Commune has given us.<sup>21</sup>

The above passage seems to suggest that all workers, regardless of function or accomplishment, would have to be contented with the wages of ordinary labor, but this is not the impression usually given in descriptions of the dictatorship of the proletariat. In this transition stage of society, every person who desires to receive an income must work for wages as an employee of the proletarian state. He who does not work will be expected to refrain from eating as well. But, according to most versions, each worker will receive from society in wages as much as he has given it in terms of productiveness. Wages will not be equal from worker to worker but will vary with the accomplishments of the workers. On the whole, however, inequality in the distribution of income will be very small in comparison with that which formerly existed under capitalism. The unequal distribution of income under the dictatorship will be far from ideal, according to the Marxian school of thought, but it cannot be avoided in the transition period. As Lenin said:

The first phase of Communism, therefore still cannot produce justice and equality, differences, and unjust differences, in wealth will still exist, but the *exploitation* of man by man will have become impossible, because it will be impossible to seize as private property the *means of production*, the factories, machines, land, and so on.<sup>22</sup>

The unequal distribution of income, like some other features of the new stage of society which are not entirely desirable, indicates merely that the new society is "one which is just *emerging* from capitalist society, and which therefore in all respects—economic, moral and intellectual—still bears the birthmarks of the old society from whose womb it sprung."<sup>23</sup>

In any case, the chief significance of the dictatorship of the proletariat is as a period of preparation for the ideal state of society which is to follow. The chief task is that of molding the individual

<sup>21</sup> *Ibid.*, p. 156. Reprinted by permission of the Vanguard Press, New York.

<sup>22</sup> Cited in *Handbook of Marxism*, p. 179. Reprinted by permission of Random House, New York.

<sup>23</sup> *Ibid.*, p. 748. Reprinted by permission of Random House, New York.

citizens so that they will become ready for the ideal system, and the proletarian state is to be quite ruthless in this preparatory work. After the dictatorship has been in operation for a time, nonconformity in the behavior of individual citizens will be

a rare exception, and will probably be accompanied by such swift and severe punishment (for the armed workers are men of practical life, not sentimental intellectuals, and they will scarcely allow anyone to trifl with them), that very soon the *necessity* of observing the simple, fundamental rules of every-day social life in common will have become a *habit*. The door will then be open for the transition from the first phase of communist society to its higher phase.<sup>24</sup>

*The Russian Dictatorship* The Russian revolution, while it did not result from conditions which conformed at all strictly to those predicted by Marx, was satisfactory enough to some modern Marxians as an example of the working out of the Marxian predictions. In similar fashion, the present situation in Russia is quite acceptable to these same people as an example of the dictatorship of the proletariat. Though they are conscious of the fact that practically all the powers which are supposed to reside in the proletariat are wielded actually by that small minority known as the Communist Party in Russia, and even more specifically by the small group of leaders of the Communist Party, they contend that this situation is both necessary and desirable. The proletariat as a whole is too large and unwieldy to exercise direct control over the government and the economic system, and must necessarily delegate its powers to a smaller group, the vanguard of the proletariat, found in the Communist Party and its leaders. The Communist Party would have no function or reason for being if it were compelled to follow along like the tail on the proletarian dog, where the great masses of the proletariat led. Moreover, trying to carry on a government and economic system by means of a proletariat without the Communist Party at its head would be like trying to fight a war by means of a mass army which lacked a general staff.

Although great powers are actually wielded by the Communist Party, and its leaders, these agencies, according to this point of view, are responsible in the last analysis to the proletariat as a whole. The heads of the Communist Party are merely leaders, not dictators. They convince the rank and file as to the wisdom of their decisions and do not merely coerce the masses into following along. Unless

<sup>24</sup> *Ibid* p. 759 Reprinted by permission of Random House New York

the leaders lead the masses in the direction of the goals desired by the people, they cannot maintain their position of leadership As Lenin once stated the matter

Among the masses of the people, we communists are but drops in the ocean, and we cannot rule unless we give accurate expression to the folk consciousness Otherwise the Communist Party will not be able to lead the proletariat, the proletariat will not be able to lead the masses, and the whole machine will fall to pieces<sup>25</sup>

Many people, however, are unable to accept this point of view It seems to them that the powers which should belong to the proletariat as a whole are far too greatly concentrated in the Communist Party, in the leaders of the Party, and in one man, Stalin himself It also seems that this leadership by the dictator or by a small minority of the Party is often quite irresponsible It seems, in other words, that the masses are forcibly led in the directions which seem desirable to the leader or leaders and not in the directions which the masses would choose if they were allowed to express themselves freely and openly Thus, according to this viewpoint, the situation in Russia is one of dictatorship over the proletariat and not dictatorship of the proletariat If this is true, it is quite possible that an effort will be made to perpetuate the dictatorship and that Russia will not ripen into the ideal stage of full communism at all rapidly

### *Full Communism*

The final stage of full communism does not follow automatically from the dictatorship of the proletariat with the mere passage of time It will come only when and if the economic system and its people are ready for it, and quite a little is involved in the process of getting ready In the first place, all traces of the old capitalistic ideology must be stamped out Individuals must forget that there was ever a time when income could be derived from the mere ownership of property as well as from productive labor They must forget that some people once got very large incomes while others received small ones They must lose any hope of differential rewards for differences in productivity or service They must forget all about differences in skill, training, and mental or physical abilities They

<sup>25</sup> J. Stalin, *Leninism*, Volume I New York International Publishers 1938, p. 51

must come around to the notion that, if a man does the best he can in the best type of work for which he is fitted, he is just as good and just as deserving of income as any other man, regardless of differences in productivity and output. They must give up their old acquisitive and self-seeking types of behavior and become socially minded so that they will both work as hard as they can for the benefit of society as a whole and be content to receive, as a reward for their work, an amount of income based on their needs in consumption.

These changes in human beings and their thinking must be accompanied, apparently, by a great expansion of production before the stage of full communism can be reached. If the ideal society is to dispense with markets, money, and prices and allow each individual who works as best he can to help himself to commodities and services on the basis of his needs, the outputs of many kinds of economic goods will have to be expanded enormously. The outputs of goods which capitalism produces today would be quite inadequate for the satisfaction of human wants if the price tags were removed and individuals were allowed to help themselves freely to the available goods.

*The Withering Away of the State* After these developments have taken place a stage of society will be reached in which class distinctions and antagonisms have been eliminated. There will no longer be any economic or social basis for distinguishing one individual or group of individuals from another. As a result, the state, which is always an agency of oppression, will have lost its function and will wither away and disappear. There must be at least two classes, with the one capable of oppressing the other, in order for the state to have significance as an agency of oppression. When all individuals in the society have precisely the same status, there is no one to oppress and no one to be oppressed. The state is not abolished. It merely atrophies and disappears.

As Lenin described this development:

Only in Communist society, when the resistance of the capitalists has been completely broken, when the capitalists have disappeared, when there are no classes (i.e., there is no difference between the members of society in their relation to the social means of production), only then "the state ceases to exist," and "it becomes possible to speak of freedom." Only then a really full democracy, a democracy without any exceptions, will be possible and will be realized. And only then will democracy itself begin to wither away due to the simple fact that, freed from capitalist

slavery, from the untold horrors, savagery, absurdities and infamies of capitalist exploitation, people will gradually become accustomed to the observation of the elementary rules of social life that have been known for centuries and repeated for thousands of years in all school books, they will become accustomed to observing them without force, without compulsion, without subordination, without the *special apparatus for compulsion* which is called the state.<sup>26</sup>

And again

Finally, only Communism renders the state absolutely unnecessary, for there is *no one* to be suppressed—"no one" in the sense of a *class*, in the sense of a systematic struggle with a definite section of the population. We are not Utopians, and we do not in the least deny the possibility and inevitability of excesses on the part of *individual persons*, nor the need to suppress *such excesses*. But in the first place, no special machinery, no special apparatus of repression is needed for this, this will be done by the armed people itself as simply and as readily as any crowd of civilized people, even in modern society, parts a pair of combatants or does not allow a woman to be outraged. And, secondly, we know that the fundamental social cause of excesses which consists in violating the rules of social life is the exploitation of the masses, their want and their poverty. With the removal of this chief cause, excesses will inevitably begin to "wither away." We do not know how quickly and in what succession, but we know that they will wither away. With their withering away, the state will also wither away.<sup>27</sup>

**Government and the Control of Economic Activity** But, if the state withers away, how will the economy of full communism operate? There are no private enterprises to take responsibility for the guidance of production and there are no money price and cost relationships to serve as the basis for economic decision-making. On the other hand, a full-fledged system of economic planning, which is the alternative to operation on the basis of the price system, would seem to require the existence not only of government but of a strong central government with power to make and enforce the plans. Of course, one might argue that each individual will be so changed and will become so socially minded under full communism that he will take his appropriate place in the productive scheme of society as a whole without any guidance being necessary. Each individual will be guided as by an inner light (or an invisible hand) to enter that occupation in which he can be most useful to society, and

<sup>26</sup> Quoted in *Handbook of Marxism*, pp. 745-746. Reprinted by permission of Random House, New York.

<sup>27</sup> *Ibid.*, p. 747. Reprinted by permission of Random House, New York.

the system will operate automatically to satisfy the wants of the citizens as consumers To the vulgar economist, it seems amazingly utopian to think that the economic system could operate at all in this fashion, and that it could operate more efficiently than capitalism to an extent which would make it possible for all individuals to help themselves freely to commodities and services seems altogether out of the question Even if such an anarchistic economic system could operate without having chaos as its leading product, it would probably be a thoroughly static and unprogressive economic system

One other escape from this dilemma remains open In view of the distinction between the state and the government, it might be possible for the state as an agency of oppression to wither away, while the government, as the machinery for guiding the cooperative activities of the individual citizens, might remain This might make it possible for the system of full communism to operate as a planned economy without any individual or groups of individuals being oppressed However, this solution appears to be denied by the words of Lenin when he says that under full communism the government will finally become completely democratic, but that democracy itself will then proceed to wither away On the other hand, it is sometimes suggested that Marx was an authoritarian and centralizing communist and that he conceived of full communism as operating on the basis of economic planning through a system of voluntary centralism That is, the central government would have large powers in the economic sphere but these powers would be voluntarily accorded to it by the decisions of the masses of people and would not be imposed upon the people from above

*Other Economic Matters under Full Communism* Many of these difficulties of interpretation arise out of the fact that Marx and Engels, and even then modern interpreters, speak of the system of full communism only in rather general terms For example Marx said of this ideal system

In the higher phase of Communist society, after the enslaving subordination of the individual under the division of labor has disappeared, and therewith also the opposition between manual and intellectual labor, after labor has become not only a means of life but also the highest want in life, when, with the development of all the faculties of the individual, the productive forces have correspondingly increased, and all the springs of social wealth flow more abundantly—only then may the limited horizon of capitalist right be left behind entirely, and society inscribe on its

banners "From everyone according to his faculties, to everyone according to his needs"<sup>28</sup>

As this general prospectus is usually interpreted, the system of full communism will involve the complete disappearance of private property. Both productive wealth and consumers' goods will be owned by the entire social group. Some consumers' goods must pass into private possession for purposes of final consumption, but the basic title to them always remains social. Individuals work for society as a whole and produce as much as they can. Then products belong to society as a whole. These products are not exchanged, or bought and sold, and money and prices will have disappeared. Commodities are stored at various central places and all individuals who work may help themselves to the commodities on the basis of needs. They have no incentive to take more than they need at any one time because, in the face of the superabundance of commodities, they can replenish their supplies at will. Services are also dispensed at convenient places and individuals may receive them as needed. This is all there is to the distribution of income. There is no question of wages, interest, rent, and profits. In this situation, life is simple and yet full and pleasant. The individual has plenty of leisure and opportunity to indulge in the higher forms of pleasure and culture. No one owns anything, and yet everyone is rich.

*Difficulties to Be Encountered.* Although the system of full communism sounds most attractive to some people, there are some rather obvious obstacles to its attainment. In the first place, there is the question of incentives. If there are no differentials in income on the basis of ability, skill, training, and productivity, how do we get individuals to select the highest type of work for which they are qualified and work to the best of their ability in such occupations? Judging people on the basis of their actions under the capitalistic system, it would be expected that, under full communism, some individuals would work most industriously while a much larger number of individuals would just as industriously stand around and watch them, or merely go through the motions of working. But, the communists would say, this is precisely the trouble with the bourgeois economist. He does not see how plastic human nature is and how profoundly people themselves will be changed under full communism. People will work according to their abilities.

<sup>28</sup> Karl Marx. *The Gotha Program*, p. 31. Reprinted by permission of the New York Labor News Company.

without any doubt if, as Marx put it, labor has become not only a means of life but the highest want in life Moreover, people will be content to receive income on the basis of their needs without regard for differences in ability, types of work, or productivity Here the bourgeois economist can only reply that he will believe all this after some country has taken the plunge and has shown that it can operate successfully on the basis of full communism

Again, what are the prospects of producing enough commodities and services so that individuals can be allowed to help themselves freely to them on the basis of needs? We do not deny for a moment that most capitalistic systems usually fail to produce the maximum possible quantity of commodities and services which could be turned out with the available productive resources, but it is difficult to see how, under any economic system, production could be increased so greatly that scarcity would disappear, all commodities and services would become free goods, and human wants would be completely satisfied Since no one contends that our capitalistic system is less than 50 per cent efficient, we could hardly look for more than a doubling of production under any other system, and it seems to us that a mere doubling of ordinary production would fall well short of the complete satisfaction of human wants And there might be a further question as to whether the complete satisfaction of human wants in the economic field is a desirable objective in the first place Would life be worth living if our economic wants were completely satisfied? Now it may be that we have been misinterpreting the objectives of full communism Perhaps there is no intention of satisfying all human wants as they exist today, and the objective of full communism is merely to satisfy all human needs as distinguished from wants That is, it might be argued that many human wants today are of a social character and depend for their existence on the type of society in which we live Under full communism, human wants would be much less extensive and complicated and would correspond closely to the category of needs Under this interpretation, the production of enough goods so that they could be freely distributed on the basis of needs would seem more nearly feasible, but even this result would depend upon the existence of adequate incentives for the individuals of the system as producers The success of this system of distribution would also seem to depend upon the disappearance of the acquisitive element in human nature so that no one would take more goods than he needed im-

mediately This matter would become especially important if any particular goods existed from time to time in quantities insufficient to satisfy the needs of everyone

*The Length of the Transition Period* On the basis of this discussion, we may be led to wonder how long it will be, according to the Marxian theorists, before the transition stage of the dictatorship of the proletariat can come to an end and the ideal stage of full communism can be reached Estimates on this point have varied widely Marx seems to have been fairly optimistic when he said "You will have to go through fifteen, twenty, or even fifty years of civil and international war, not only to change relationships but also to change your own selves, to render yourselves fit to assume the political reins" <sup>29</sup> Lenin, on the other hand, took a much darker view of the situation when he wrote

Under the dictatorship of the proletariat, we will have to educate millions of peasants and petty proprietors, hundreds of thousands of office workers, officials, and bourgeois intellectuals, to subordinate all these to the proletarian state and to proletarian leadership, to overcome their bourgeois habits and traditions to re-educate in a protracted struggle, under the controlling auspices of the dictatorship of the proletariat, the proletarians themselves, for they will not be able to rid themselves of their own petty bourgeois prejudices at the first stroke as if by magic, or at the behest of the Virgin Mary, or by a slogan, resolution or decree, it can be done only in the course of a long and difficult mass struggle against the mass of petty bourgeois influences <sup>30</sup>

On the basis of Lenin's statement it would not be surprising if Russia were still in the dictatorship of the proletariat (if that is the stage she is in now) after another century or two And even this would not necessarily discredit the Marxian notion that the stage of full communism will replace the dictatorship of the proletariat when the time is ripe We must remember that in such matters twenty years may count only as one day

### *The Role of the Communist Party*

In all the developments which Marx predicted, the Communist Party was to have a most important part As long as the capitalistic system managed to keep on operating, the Party was to carry on

<sup>29</sup> J. Stalin, *Foundations of Leninism*, pp. 47-48 Reprinted by permission of International Publishers, New York  
<sup>30</sup> *Ibid.*, p. 48 Reprinted by permission of International Publishers, New York

the work of arousing and educating the proletariat. In the absence of this work, the proletariat would remain unorganized, lacking in class-consciousness, politically ignorant, and infected with all manner of bourgeois ideas. When properly aroused and educated, the proletariat would be ready to take over the state, government, and economic system when the capitalistic system broke down and the day of revolution came. Of course, the unpreparedness of the proletariat would not keep the capitalistic system from breaking down, but in such a case the breakdown would produce chaos rather than a period of transition and preparation out of which would eventually emerge the perfect society.

Having tutored and coached the proletariat up to the time of the revolution, the Communist Party could not be expected to withdraw its influence during the dictatorship of the proletariat. On the contrary, the Communist Party would still be the vanguard of the proletariat during the transition period. It would serve as a kind of military general staff for the proletariat and would occupy a dominant position in the governmental machinery of the dictatorship. In theory, at least, it would maintain its position of leadership by leading the proletariat toward the objectives desired by the proletariat. Still later, when the ideal stage of full communism had been reached and the state had withered away, the Communist Party would presumably wither away too, with its functions performed and its duties done.

#### QUESTIONS

- 1 Why did Marx think that a revolution would be necessary in order that the capitalistic system might pass into the dictatorship of the proletariat?
- 2 "Marx changed his mind more than once as to the capitalistic country in which the revolution would occur first." Explain.
- 3 When, according to Marx, might the revolutionary overthrow of capitalism be expected to occur?
- 4 How can it be determined, according to Marx, when economic conditions under capitalism are ripe for revolution?
- 5 Explain the political and economic features of the dictatorship of the proletariat.
- 6 How does the economic system which Marx foresaw under the dictatorship of the proletariat differ from the system which modern socialists are anxious to set up? Explain.

- 7 "The present economic and political system of Soviet Russia is a good example of what Marx meant by the dictatorship of the proletariat." Do you agree? Explain
- 8 What conditions were necessary, according to Marx, in order that an economic system might pass from the dictatorship of the proletariat to complete communism? Explain
- 9 What political and governmental changes are involved in the transition from the dictatorship of the proletariat to full communism?
- 10 Distinguish between the two stages of society which Marx thought would follow upon the breakdown of capitalism and the revolution, emphasizing both economic and political features
- 11 "While he was specific enough in criticizing capitalism, Marx was rather vague and indefinite in describing his own ideal system" Show whether you agree
- 12 Discuss the problems which are involved in operating the economic system of full communism
- 13 How long will it take, according to Marx, for the dictatorship of the proletariat to pass into the ideal system of full communism?
- 14 Discuss the role of the Communist Party under capitalism, and after the revolution



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